
GLOBALIZATION IMPERATIVE



CHAPTER OVERVIEW

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Marketing products and services around the world, transcending national and political boundaries, is a fascinating phenomenon. The phenomenon, however, is not entirely new. Products have been traded across borders throughout recorded civilization, extending back beyond the Silk Road that once connected East with West from Xian to Rome on land, and the recently excavated sea trade route between the Roman Empire and India that existed 2,000 years ago. However, since the end of World War II, the world economy has experienced a spectacular growth rate never witnessed before in human history, primarily led by large U.S. companies in the 1950s and 1960s, then by European and Japanese companies in the 1970s and 1980s, and most recently by new emerging market firms, such as Lenovo, Mittal Steel, and Cemex. In particular, competition coming recently from the so-called BRIC countries (Brazil, Russia, India, China) has given the notion of global competition a touch of extra urgency and significance that you see almost daily in print media such as the *Wall Street Journal*, *Financial Times*, *Nikkei Shimbun*, and *Folha de São Paulo*, as well as in TV media such as BBC, NBC, and CNN. With a few exceptions, such as Korea's Samsung Electronics (consumer electronics) and China's Haier (home appliances), most emerging-market multinational companies are not yet household names in the industrialized world, but from India's Infosys Technologies (IT services) to Brazil's Embraer (light jet aircrafts), and from Taiwan's Acer (computers) to Mexico's Cemex (building materials), a new class of formidable competitors is rising.¹

¹“A New Threat to America Inc.” *Business Week*, July 25, 2005, p. 114; and also read Martin Roll, *Asian Brand Strategy: How Asia Builds Strong Brands*, New York: Palgrave Macmillan, 2006.

In this chapter, we will introduce to you the complex and constantly evolving realities of global marketing. Global marketing refers to a strategy for achieving one or more of four major categories of potential globalization benefits: cost reduction, improved quality of products and programs, enhanced customer preference, and increased competitive advantage on a global basis. The objective is to make you think beyond exporting and importing. As you will learn shortly, despite wide media attention to them, exporting and importing constitute a relatively small portion of international business. We are not saying, however, that exporting and importing are not important. In 2006, the volume of world merchandise trade grew by 8 percent, while world gross domestic product recorded a 3.5 percent increase, which confirms that the trend in world merchandise trade grows by twice the annual growth rate of output since 2000. Total merchandise trade volume reached \$16.3 trillion in 2008, compared to \$6 trillion in 2000.² In recent years, improved market conditions in the United States and Europe, as well as strong growth in the Emerging Markets, such as China and India, steadily improved the world economy after the devastating terrorist attacks in the United States on September 11, 2001. However, the aftermath of the U.S.-led war against Iraq, the high oil prices, and most recently, the unprecedented global recession triggered by the subprime mortgage crisis in the United States in 2008, among other things, continue to curb a full-fledged recovery in the world economy. Indeed, at the time of this writing in early 2009, as the global economy is currently experiencing the worst recession since the Great Depression of 1929–1932, World Bank predicts that the world trade volume will shrink in 2009 for the first time in over 25 years,³ and the specter of economic nationalism—the country’s urge to protect domestic jobs and keep capital at home instead of promoting freer international trade—is hampering further globalization.⁴ Although sometimes bumpy, it is expected that the drive for globalization will continue to be promoted through more free trade, more Internet commerce, more networking of businesses, schools and communities, and more advanced technologies.⁵

◆ ◆ ◆ ◆ ◆ ◆ ◆ ◆ ◆ ◆ WHY GLOBAL MARKETING IS IMPERATIVE

We frequently hear terms such as *global markets*, *global competition*, *global technology*, and *global competitiveness*. In the past, we heard similar words with *international* or *multinational* instead of *global* attached to them. What has happened since the 1980s? Are these terms just fashionable concepts of the time without some deep meanings? Or has something inherently changed in our society?

Saturation of Domestic Markets. First, and at the most fundamental level, the saturation of domestic markets in the industrialized parts of the world forced many companies to look for marketing opportunities beyond their national boundaries. The economic and population growths in developing countries also gave those companies an additional incentive to venture abroad. Now companies from emerging economies, such as Korea’s Samsung and Hyundai and Mexico’s Cemex and Grupo Modelo, have made inroads into the developed markets around the

²*The World Factbook 2009*, <https://www.cia.gov/library/publications/the-world-factbook/index.html>.

³World Bank, *Global Economic Prospect 2009*, www.worldbank.org/gep2009.

⁴“The Return of Economic Nationalism,” *Economist*, February 7, 2009, pp. 9–10.

⁵The reader needs to be cautioned that there may be limits to the benefit of globalization for two primary reasons. First, firms in poor countries with very weak economic and financial infrastructures may not be able to (afford to) adjust fast enough to the forces of globalization. Second, poor countries could be made worse off by trade liberalization because trade tends to be opened for high-tech goods and services exported by rich countries – such as computers and financial services – but remains protected in areas where those poor countries could compete, such as agricultural goods, textiles or construction. See, for example, Joseph E. Stiglitz, *Globalization and Its Discontents*, New York: W.W. Norton & Co., 2003. For an excellent treatise on various paradoxes of globalization, refer to Terry Clark, Monica Hodis, and Paul D’Angelo, “The Ancient Road: An Overview of Globalization,” in Masaaki Kotabe and Kristiaan Helsen, ed., *The SAGE Handbook of International Marketing*, London: Sage Publications, 2009, pp. 15–35.

world. The same logic applies equally to companies from developed countries, such as Australia and New Zealand, geographically isolated from the other major industrialized parts of the world. Dôme Coffees Australia is building a multinational coffee shop empire by expanding into Asia and the Middle East. Inevitably, the day will come when Starbucks from the United States and Dôme Coffees from Australia will compete head-on for global dominance.⁶

Emerging Markets. During the twentieth century, the large economies and large trading partners have been located mostly in the Triad Regions of the world (North America, Western Europe, and Japan), collectively producing over 80 percent of world gross domestic product (GDP) with only 20 percent of the World's population.⁷ However, in the next 10 to 20 years, the greatest commercial opportunities are expected to be found increasingly in ten Big Emerging Markets (BEMs)—the Chinese Economic Area, India, Commonwealth of Independent States (Russia, Central Asia, and Caucasus states), South Korea, Mexico, Brazil, Argentina, South Africa, Central European countries, Turkey, and the Association of Southeast Asian Nations (Indonesia, Brunei, Malaysia, Singapore, Thailand, the Philippines, and Vietnam). Accordingly, an increasing number of competitors are expected to originate from those ten emerging economies. In the past 20 years, China's real annual GDP growth rate has averaged 9.5 percent a year; while India's has been 5.7 percent, compared to the average 3 percent GDP growth in the United States. Clearly, the milieu of the world economy has changed significantly and over the next two decades the markets that hold the greatest potential for dramatic increases in U.S. exports are not the traditional trading partners in Europe, Canada, and Japan, which now account for the overwhelming bulk of the international trade of the United States. But they will be those BEMs and other developing countries that constitute some 80 percent of the "bottom of the pyramid."⁸ As the traditional developed markets have become increasingly competitive, such emerging markets promise to offer better growth opportunities to many firms.

Global Competition. We believe something profound has indeed happened in our view of competition around the world. About thirty years ago, the world's greatest automobile manufacturers were General Motors, Ford, and Chrysler. Today, companies like Toyota, Honda, BMW, Renault, and Hyundai, among others, stand out as competitive nameplates in the global automobile market. Now with a 15-percent market share in the United States, Toyota's market share is larger than Ford's 14 percent. In early 2008, Toyota surpassed General Motors to become the world's largest automaker in terms of worldwide output.⁹ Similarly, while personal computers had been almost synonymous with IBM, which had previously dominated the PC business around the world, today, the computer market is crowded with Dell and Hewlett-Packard (HP) from the United States, Sony and Toshiba from Japan, Samsung from Korea, Acer from Taiwan,¹⁰ and so on. Indeed, Lenovo, a personal computer company from China, acquired the IBM PC division in 2005, and now sells the ThinkPad series under the Lenovo brand. The deal not only puts Lenovo into third place in the industry, it also challenges the world top players, Dell and HP/Compaq, respectively.¹¹ Nike is a

⁶"Bean Countess," *Australian Magazine*, December 9–10, 2000, p. 50+.

⁷L. Bryan, *Race for the World: Strategies to Build A Great Global Firm*, Boston, MA: Harvard Business School Press, 1999.

⁸C. K. Prahalad, *The Fortune at the Bottom of the Pyramid: Eradicating Poverty through Profits*, Philadelphia, PA: Wharton School Publishing, 2004.

⁹"Toyota's Global Sales Top GM by 277,000 Units in 1st Half," Nikkeinet Interactive, www.nni.nikkei.co.jp, July 24, 2008. Catches GM in Global Sales," CNNMoney.com, January 23 2008.

¹⁰"Why Taiwan Matters: The Global Economy Couldn't Function without It, but Can It Really Find Peace with China?" *Business Week*, May 16, 2005, pp. 74–81.

¹¹"Can China's Lenovo Brand in the Land of Dell?" *B to B*, October 10, 2005, p. 1 and p. 45.



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Globe-trotting companies are vying for customers' "mind share" in many parts of the world such as in Piccadilly Circus, London, England.

U.S. company with a truly all-American shoe brand, but all its shoes are made in foreign countries and exported to many countries. Pillsbury (known for its Betty Crocker recipes and Häagen-Dazs ice cream brand) and 7-Eleven convenience stores are two American institutions owned and managed, respectively, by Diageo from the United Kingdom and Seven & i Holdings Co. from Japan. On the other hand, the world of media, led by U.S. media giants, has become equally global in reach. MTV, targeting teenage audiences, has 35 channels worldwide, 15 of them in Europe, produces a large part of its channel contents locally. CNN has 22 different versions. In 1996, 70 percent of the English-language version of CNN International was American; today that share has shrunk to about 8 percent.¹² The video game industry is truly global from day one; Nintendo's Wii, Sony's Playstation 3, and Microsoft's Xbox now vie for customers in the Triad regions simultaneously.

Global Cooperation. Global competition also brings about global cooperation. This is most obvious in the information technology industry. IBM and Japan's Fujitsu used to be archrivals. Beginning in 1982, they battled each other for fifteen years in such areas as software copyright. But in October 2001, they developed a comprehensive tie-up involving the joint development of software and the mutual use of computer technology. IBM would share its PC server technology with Fujitsu and the Japanese company would supply routers to IBM.¹³ Japan's Sony, Toshiba, and U.S. computer maker IBM are jointly developing advanced semiconductor processing technologies for next-generation chips. As part of the project, IBM transfers its latest technologies to Sony and Toshiba, and the partner companies each send engineers to IBM's research center in New York to work on the joint project.¹⁴ Similarly, in the automotive industry, in 1999 French carmaker Renault SA took a 36.8 percent stake in Japanese carmaker Nissan Motor Corp. The two companies began producing cars on joint platforms in 2005. To help pave the way for that, in March, 2001 the two carmakers decided that they would combine their procurement operations in a joint-venture company that would eventually handle 70 percent of the companies' global purchasing. The joint venture is headquartered in Paris, with offices in Japan and the United States.¹⁵

¹²"Think Global," *Economist*, April 11, 2002.

¹³"Fujitsu, IBM Negotiate Comprehensive Tie-up," *Nikkei Interactive Net*, www.nni.nikkei.co.jp, October 18, 2001.

¹⁴"IBM, Sony, Toshiba Broaden and Extend Successful Semiconductor Technology Alliance," IBM Press Room, <http://www-03.ibm.com/press/us/en/pressrelease/19103.wss>, January 12, 2006," *Nikkei Interactive Net*, www.nni.nikkei.co.jp, April 2, 2002.

¹⁵"Nissan and Renault Look to Boost Joint Procurement Efforts," *Japan Times*, November 29, 2002.

Internet Revolution. The proliferation of the Internet and e-commerce is wide reaching. The number of Internet users in the world reached 1.4 billion by March 2008, which amounts to almost three times that of 2000. According to Internet World Stat,¹⁶ 41.2 percent of the Internet users come from Asia, followed by 24.6 percent and 15.7 percent from Europe and North America, respectively. Although the Middle East and Africa account for only 6.3 percent of Internet users, these two regions rank top two in their usage growth of over ten times between 2000 and 2008. In the same period, Internet usage in Asia and Latin America/Caribbean grew by 475 percent and 861 percent, respectively. As a result, the total global e-commerce turnover ballooned more than 33 times from \$385 billion in 2000 to \$12.8 trillion in 2006, taking up 18 percent of the global trade of commodities in 2006. Developed countries led by the United States are still leading players in this field, while developing countries like China are emerging, becoming an important force in the global e-commerce market.¹⁷

Compared to business-to-consumer (B2C) e-commerce, business-to-business (B2B) e-commerce is larger, growing faster, and has less unequal geographical distribution globally.¹⁸ Increases in the freedom of the movements of goods, services, capital, technology, and people, coupled with rapid technological development, resulted in an explosion of global B2B e-commerce. The share a country is likely to receive of the global B2B e-commerce, on the other hand, depends upon country-level factors such as income and population size, the availability of credit, venture capital, and telecom and logistical infrastructure; tax and other incentives, tariff/nontariff barriers, government emphasis on the development of human capital, regulations to influence firms' investment in R&D, organizational level politics, language, and the activities of international agencies.¹⁹

Who could have anticipated the expansion of today's e-commerce companies, including Amazon, eBay, and Yahoo in the United States; QXL Ricardo and Kelkoo in Europe; Rakuten and 7dream in Japan, and Baidu in China? The Internet opened the gates for companies to sell direct-to-consumers easily across national boundaries. Many argue that e-commerce is less intimate than face-to-face retail; however, it actually provides more targeted demographic and psychographic information.

Manufacturers that traditionally sell through the retail channel may benefit the most from e-commerce. Most importantly, the data allow for the development of relevant marketing messages aimed at important customers and initiate loyal relationships on a global basis.²⁰ With the onset of satellite communications, consumers in developing countries are equally familiar with global brands as consumers in developed countries, and as a result, there is tremendous pent-up demand for products marketed by multinational companies (which we also refer to as MNCs).²¹

What's more, the Internet builds a platform for a two-way dialogue between manufacturers and consumers, allowing consumers to design and order their own products from the manufacturers. Customized build-to-order business model is already an established trend. Dell Computer is a pioneer that does business globally by bypassing traditional retail channels. It accepts orders by phone, fax, or on the Internet.²² General Motors started providing a build-to-order Web service for its

¹⁶<http://www.internetworldstats.com>, accessed July 20, 2009.

¹⁷Annual Report on the Development of Global E-Commerce Industry: 2006-2007, http://market.cidnet.com/pub/report/show_17192.html, accessed July 20, 2009.

¹⁸B2B and B2C, among others, have become trendy business terms in recent years. However, they are fundamentally the same as more conventional terms, consumer marketing and industrial marketing, respectively, except that B2B and B2C imply the use of the Internet, Intranet, customer relationship management software, and other information technology expertise. In our book, we will not use these trendy terms unless they are absolutely necessary in making our point.

¹⁹Nikhilesh Dholakia, "Determinants of the Global Diffusion of B2B E-commerce," *Electronic Markets*, 12 (March 2002), pp. 120-29.

²⁰Andrew Degenholtz, "E-Commerce Fueling the Flame for New Product Development," *Marketing News*, March 29, 1999, p. 18.

²¹D. J. Arnold, and J. Quelch, "New Strategies in Emerging Markets," *Sloan Management Review* 40(1), 1998, pp. 7-20.

²²However, Dell's direct sales on the Internet fails to work in some emerging markets, particularly where customers want to see products before they buy. Such is the case in small cities in China. See "Dell May Have to Reboot in China," *Business Week*, November 7, 2005, p. 46.

Brazilian customers in 2000. Mazda's Web Tune Factory site, being one of the first Japanese auto build-to-order models, allows consumers to choose their own engine specifications, transmission type, body color, wheel design and other interior and exterior equipment.²³ However, as presented in **Global Perspective 1-1**, we would also like to stress as a caveat that the proliferation of e-commerce and satellite communications does not necessarily mean that global marketing activities are going culture- and human contact-free. Learning of foreign languages will probably remain as important as ever.



GLOBAL PERSPECTIVE 1-1

THE INTERNET WORLD AND CULTURAL AND HUMAN ASPECTS OF GLOBAL MARKETING

Cultural differences greatly affect business relationships in the world of e-commerce, but this is often underestimated, especially in international team-building efforts. Language issues are not the only source of the problem. Foreign companies need acceptance by the local market and understanding of the local business culture. The Internet's awesome communications power can be turned into a conduit for miscommunication if such cultural factors are ignored. Knowing what level of communication is appropriate for a certain level of trust is particularly important in a Web-based environment, where face-to-face contact may be more limited.

Think, for example, a typical mid-sized manufacturer in, say, Taiwan, China, or Thailand. Would it enter into a strategic business relationship with companies and people they encounter only through computerized interactions? The short answer is yes; they will enter into such relationships. However, we qualify our positive reply by adding that the initial courtship ritual must continue to have personal face-to-face, one-to-one, or what we feel is becoming a new "screen-to-screen" relationship dimension as with a traditional business model. In China, which has a long tradition of distrust and a culture of relationship building known as "guanxi," information, a key source of power in this business culture, is only passed selectively to individuals who are proven trustworthy or known as insiders. This kind of culture has considerable impact on B2B e-commerce adoption and diffusion in China. In this context, such sociocultural tensions cannot be solved with only the Internet's technical power. In fact, traditional personal face-to-face communications are still critical in building trust and relationships.

However, after the initial mating ritual, you can and already do see tremendous transactional business-to-business activity

Sources: Frank Cutitta, GINLIST@LIST.MSU.EDU, April 17, 1999; Nitish Singh, Vikas Kumar, and Daniel Baack, "Adaptation of Cultural Content: Evidence from B2C E-Commerce Firms," *European Journal of Marketing*, 39 (1/2), 2005, pp. 71–86; Jing Tan, Katherine Tyler, Andrea Manica, "Business-to-Business Adoption of eCommerce in China," *Information & Management*, 44, April 2007, pp. 332–51; and Maris G. Martinsons, "Relationship-Based e-Commerce: Theory and Evidence from China," *Information Systems Journal*, published online, April 15, 2008.

in these countries. There is nothing to say that e-commerce can or should replace the human element in relationship building. In fact, e-commerce is a new form of personalized relationship building that even the highest context cultures engage in. eBay and the other online auction companies are perfect examples of such new electronic relationship and trust building. Even in the Eastern cultures, we see numerous gambling sites springing up where the only aspects of the relationship are anonymous e-commerce-related.

The critical factor will be the Web site evolving into the first step in developing the personal international business relationship. Unless the Web site makes the first connection based on sensitivity to the cross-cultural aspects of interface design, human factors, navigation currency, time and date conventions, localization, internationalization, and so on, the ability to "connect" will be stilted.

In the information technology sector, one can look at Dell and Gateway, which both do very strong business in the Asia/Pacific region. The networking company, Cisco Systems, serves as an example of the morphing of electronic and personal relationships. While they have done a tremendous job of building global relationships and partnerships on an in-country face-to-face level, almost 90 percent of their business (i.e., sales transactions) is conducted over the Web.

Has the Web replaced the need for the personal business courtship? Absolutely not. Has it added a new element to the same relationship after the bonds are formed? Most definitely. Will there be new electronic forms of relationship building that replace the old model of face-to-face in a karaoke bar? . . . Yes, it is happening already. Starting with video/teleconferences in the boardroom and expanding downward to Microsoft NetMeetings using a Webcam on the desktop.

Just think, one decade or so ago very few of us would hardly dream that most Web-enabled adolescents communicate more through instant messaging than they do on the phone or in person. In ten years, technology will give us HDTV screen quality with real time audio and video bandwidth. This surely will not completely replace face-to-face interaction among global sellers and buyers, but it will for certain offer a viable substitute for those who grew up chatting online.

²³Setsuko Kamiya, "Mazda lets buyers fine-tune Rodster," The Japan Times Online, www.hapantimes.co.jp, January 5, 2002.

EXHIBIT 1-1**CHANGE IN THE WORLD'S 100 LARGEST COMPANIES
AND THEIR NATIONALITIES**

Country	1970	1980	1990	2000*	2009*
United States**	64	45	33	36	29
Germany**	8	13	12	10	15
Japan	8	8	16	23	10
France	3	12	10	7	10
Britain**	9	7	8	6	6
Italy**	3	4	4	3	5
China	0	0	0	3	5
South Korea	0	0	2	0	4
Spain	0	0	2	1	3
Netherlands**	4	5	3	6	2
Russia	0	0	0	0	2
Switzerland	2	3	3	4	1
Belgium**	0	1	1	1	1
Brazil	0	1	1	0	1
Mexico	0	1	1	1	1
Norway	0	0	0	0	1
Finland	0	0	1	0	1
Luxembourg	0	0	0	0	1
Malaysia	0	0	0	0	1
Venezuela	0	1	1	1	1
Sweden	0	0	2	0	0
Austria	0	0	1	0	0
South Africa	0	0	1	0	0
Canada	0	2	0	0	0
Australia	1	0	0	0	0
Total**	102	103	102	103	100

Source: *Fortune*, various issues up to 2009.

**Fortune* Global 500 criteria changed to include services firms (including retailing and trading)

**Includes joint nationality of firms (joint nationality has been counted for both the countries), so the total may exceed 100.

An examination of the top 100 largest companies in the world also vividly illustrates the profound changes in competitive milieu and provides a faithful mirror image of broad economic trends that we have seen over the past thirty some years (see **Exhibit 1.1**). In particular, the last decade was characterized by the long-term recession in Japan and a resurgence of the U.S. economy that had once been battered by foreign competition in the 1980s. Take Japan, which has suffered several recessions since 1995 and many political changes, as an example. The number of Japanese companies on the list fell from 23 in 2000 to 10 in 2009. The number of U.S. and European firms ranking in the largest 100 has stayed relatively stable since 1990. Although the United States boasts the largest number of firms in the top 100 list, a list of countries with large firms is getting more decentralized. One of the biggest changes since 1990 has been the emergence of China.²⁴ As economic reform progressed and Chinese companies improved their accounting standards, their presence grew steadily. Five Chinese companies are on the 2009 *Fortune Global 100* list. Because of the rising tide of petrodollars, a Chinese company, Sinopec, was lifted into the top 10 for the first time. The current world economy has changed so drastically from what it was merely a decade ago.

The changes observed in the past thirty years simply reflect that companies from other parts of the world have grown in size relative to those of the United States despite the resurgence of the U.S. economy in the 1990s. In other words, today's environment is characterized not only by much more competition from around the world but also by more fluid domestic and international market conditions than in the past. As a result, many U.S. executives are feeling much more competitive urgency in product development, materials procurement, manufacturing, and marketing around the world. It does not necessarily mean that U.S. companies have lost their competitiveness, however. The robust economy in the United States in the late 1990s met a slow down in 2000 due to

²⁴See "The China Price," *Business Week*, December 6, 2004, pp. 102-120; "How China Runs the World Economy," *Economist*, July 30, 2005, p. 11.

the crash of dot.com’s bubble economy, and was worsened by the terrorist attacks on September 11, 2001. But the strong consumer demand has saved its economy. On the other hand, many Asian countries have recovered from the 1997 Asian financial crisis (see chapter 3 for details).

The same competitive pressure equally applies to executives of foreign companies. For example, while its Japanese home market was the incredible shrinking market in the 1990s, Toyota’s new strategy has been to de-Japanize its business and make the U.S. market its corporate priority. By 2001, Toyota had already accomplished its goal by selling more vehicles in the United States (1.74 million) than in Japan (1.71 million), with almost two-thirds of the company’s operating profit coming from the U.S. market. Now Toyota’s top U.S. executives are increasingly local hires. As Mark Twain once wrote, “if you stand still, you will get run over.” This analogy holds true in describing such competitive pressure in this era of global competition.

It is not only this competitive force that is shaping global business today. Particularly in the past several years, many political and economic events have affected the nature of global competition. The demise of the Soviet Union, the establishment of the European Union and the North American Free Trade Agreement, deregulation, and privatization of state-owned industries have also changed the market environments around the world. Furthermore, the emerging markets of Eastern Europe and the rapidly re-emerging markets of Southeast Asia also add promise to international businesses.

The fluid nature of global markets and competition makes the study of global marketing not only interesting but also challenging and rewarding. The term *global* epitomizes both the competitive pressure and the expanding of market opportunities all over the world. It does not mean, however, that all companies have to operate globally like IBM, Sony, Philips, or Samsung. Whether a company operates domestically or across national boundaries, it can no longer avoid competitive pressure from other parts of the world. Competitive pressure can also come from competitors at home. When Weyerhaeuser, a forest products company headquartered in Seattle, Washington, began exporting newspaper rolls to Japan, it had to meet the exacting quality standard that Japanese newspaper publishers demanded—and it did. As a result, this Seattle company now boasts the best newspaper rolls and outperforms other domestic companies in the U.S. market as well. Even smaller firms could benefit from exacting foreign market requirements. When Weaver Popcorn Co. of Van Buren, Indiana, started to export popcorn to Japan, Japanese distributors demanded better quality and fewer imperfections. This led to improvements in Weaver’s processing equipment and product, which helped its domestic as well as international sales.²⁵ Furthermore, e-commerce comes in handy for those smaller firms with international marketing ambitions. For example, LaPebbles.com, a small handcrafted jewelry maker based in the northeastern part of the United States, can tap into potentially large global markets. So can small firms based in foreign countries looking to the U.S. market as well. Therefore, even purely domestic companies that have never sold anything abroad cannot be shielded from international competitive pressure. The point is that when we come across the term global, we should be made aware of both this intense, competitive pressure and expanding market opportunities on a global basis.



GLOBALIZATION OF MARKETS: CONVERGENCE AND DIVERGENCE

When a country’s per capita income is less than \$10,000, much of the income is spent on food and other necessity items, and very little disposable income remains. However, once per capita income reaches \$20,000 or so, the disposable portion of income increases dramatically because the part of the income spent on necessities does not

²⁵Doug LeDuc, “Overseas Markets Spur Growth for Van Buren, Ind.-Based Popcorn Maker,” *The News-Sentinel*, (April 19, 1999).

rise nearly as fast as income increases. As a result, a billion people, constituting some 16 percent of the population, around the world with per capita income of \$20,000 and above have considerable purchasing power. With this level of purchasing power, people, irrespective of their nationality, tend to enjoy similar educational levels, academic and cultural backgrounds, and access to information. As these cultural and social dimensions begin to resemble each other in many countries, people's desire for material possessions, ways of spending leisure time, and aspirations for the future become increasingly similar. Even the deeply rooted cultures have begun to converge.²⁶ In other words, from a marketing point of view, those people have begun to share a similar "choice set" of goods and services originating from many parts of the world. What does it mean?

In one sense, we see young people jogging in Nike shoes (an American product made in China), listening to System of a Down (an Armenian rock band) or Thalia Sodi (a Mexican pop singer) on Apple Computer's iPod (an American product) in Hong Kong, Philadelphia, São Paulo, Sydney, and Tokyo. Similarly, Yuppies (young urban professionals) in Amsterdam, Chicago, Osaka, and Dallas share a common lifestyle: driving a BMW (a German car assembled in Toluca, Mexico) to the office, listening to Sumi Jo's and Sissel Kyrkjebø's new CD albums (purchased on their business trips to Korea and Norway, respectively), using a Dell notebook computer (an American product made by Quanta, a Taiwanese company in Taiwan) at work, calling their colleagues with a Nokia cellular phone (a Finnish product), signing important documents with an exquisite Parker Pen (made by a French-based company owned by a U.S. company), and having a nice seafood buffet at Mövenpick (a Swiss restaurant chain) on a Friday. In the evenings, these people spend their spare time browsing various Web sites using Google search engine (an American Internet company) to do some "virtual" window-shopping on their PCs (powered by a microprocessor made in Malaysia by Intel, an American company). The convergence of consumer needs in many parts of the world translates into tremendous business opportunities for companies willing to risk venturing abroad.

The *convergence* of consumer needs at the macro level may be evident, but it does not necessarily mean that individual consumers will adopt all the products from around the world. Globalization does not suffocate local cultures, but rather liberates them from the ideological conformity of nationalism.²⁷ As a result, we have become ever more selective. Therefore, you find one of your friends at school in the United States driving a Toyota Tacoma (a compact Japanese truck made by General Motors and Toyota in Fremont, California), enjoying Whoppers at a Burger King fast food restaurant (an ex-British company, now American), and practicing capoeira (a 400-year-old Brazilian martial art); another friend in Austria is driving a Peugeot 107 (a French car made by Toyota in the Czech Republic, also marketed as Citroën 1 and Toyota Aygo), enjoying sushi at a sushi restaurant (a Japanese food), and practicing karate (an ancient Japanese martial art); and a cousin of yours is driving a Ford Escape (an American sports utility vehicle jointly developed with Mazda, a Japanese automaker), munching on pizzas (an American food of Italian origin), and practicing soccer (a sport of English origin, known as football outside the United States and some few other countries). In other words, thanks to market globalization, not only have we become more receptive to new things, but we also have a much wider, more divergent "choice set" of goods and services to choose from to shape our own individual preferences and lifestyles. This is true whether you live in a small town in the United States or in a big city in Europe. In other words, the *divergence* of consumer needs is taking place at the same time. For example, Pollo Campero, a Latin American fried chicken chain from Guatemala, which offers a crunchy bite of chicken with a Latin service in a Latin-American environment, has been catching on quietly in the United

²⁶For an excellent story about global cultural convergence, read "Global Culture" and "A World Together," *National Geographic*, 196 (August 1999), pp. 2–33.

²⁷Mario Vargas Llosa, "The Culture of Liberty," *Foreign Affairs*, issue 122, January/February 2001, pp. 66–71.

States, the land of Kentucky Fried Chicken (KFC), to cater to Americans' increased appetite for a different kind of chicken.²⁸ From a marketing point of view, it is becoming more difficult—not easier—to pinpoint consumers' preferences in any local market around the world, the more globalized the markets become.

As presented in **Global Perspective 1-2**, the European Union (EU) market offers a vivid example of how market forces of convergence and divergence are at work. One thing is clear. There is no such a thing as a static market in an era of globalization.

GLOBAL PERSPECTIVE 1-2



MARKET CONVERGENCE AND DIVERGENCE AT WORK IN THE EUROPEAN UNION

Will Euroland survive? Rejection of the proposed EU Constitution by France and The Netherlands in 2005 caused anguish for political and EU economic elites. An “ever closer union” had been seen—until the no vote called it into question—(see Chapter 2 for details), as the European answer to globalization, political security, and economic growth. European leaders aren't the only ones who are concerned. Insightful American and Japanese business managers are also worried because, contrary to popular belief, the chief economic beneficiaries of European integration are American and Japanese multinational corporations.

Historically, Europe, due to national, cultural, and ethnic differences, has had heterogeneous and fragmented markets. These markets produced small to mid-sized firms capable of adapting to, and prospering from, highly differentiated environments. Even the largest European companies tended to operate at the national, rather than Pan-European, level, avoiding the many encumbrances of functioning across borders where market conditions were so dissimilar. For instance, for many years Unilever sold a fabric softener in ten countries under seven different brand names, using a variety of marketing strategies and bottle shapes.

Typical European firms pursued niche strategies, emphasizing craftsmanship, specialization, and networks of relationships. Europe, with its myriad laws, languages, and customs, historically constituted a market environment with significant entry and operating barriers. Foreign firms could not use economies of scale or scope inherent in large homogeneous markets; they were unable to compete on the basis of low cost or low price. High labor costs, heavy taxation to support welfare states, and high expectations of European retailers and consumers, all worked together to shape an environment that favored the creation of specialized, premium products rather than mass-consumption products. This put U.S. multinationals in Europe at a competitive disadvantage.

The traditional European advantage was based on the notion that a less homogeneous marketplace requires a more individualized marketing strategy. This approach is at odds with the strategy of many American firms—preserving the ability to reduce costs through economies of scale and scope. Historically, market fragmentation shielded Europe from U.S. competition. Such fragmentation constituted location-specific advantages that

were either costly to overcome, or were simply impenetrable by many smaller U.S. companies. However, the creation of the European Union changed the rules of the game.

One major purpose of the EU is to create extensive homogeneous markets in which large European firms are able to take advantage of economies of scale and therefore are better able to compete with their U.S. counterparts. EU reformers hope to create an economy analogous to the United States, in which low inflation coexists with high growth, thereby leading to low unemployment.

The formation of the EU has resulted in extremely large levels of U.S. and Japanese foreign direct investment (FDI) in Europe. Why? First, it was feared that the EU would become “Fortress Europe” through the implementation of significant protectionist measures against firms from outside the EU. Under these circumstances, FDI constitutes tariff jumping in anticipation of negative actions that may or may not occur in the future. Second, the elimination of internal borders creates a single market, amenable to the large economies of scale and scope preferred by U.S. and Japanese multinationals.

Numbers tell the story. The average FDI inflows into the European Community (as the EU was known until November 1, 1993) amounted to \$65.6 billion from 1985–1995. The inflow in 1999 (the year the euro, a new currency adopted by eleven EU member countries, was launched) was \$479.4 billion—a 700 percent increase. By 2000 Japanese investment in the EU was roughly six times more than EU investment in Japan. In 1980 the total FDI stock of European Community was \$216 billion, by 2005 it was \$3,123 billion. Finally, FDI stock as a percentage of GDP was 8.5 percent in 1987 (the year that plans for the Maastricht Treaty were presented). In 2002, the year in which euro notes and coins replaced local currencies, it was 34.6 percent.

Four decades ago the French intellectual, J. J. Servan-Schreiber complained bitterly about the U.S. presence in Europe in a best-selling book entitled, *The American Challenge* (1967). The Europeans now face similar competitive dynamics. Ironically, in their quest for economic competitiveness, they may have made themselves more vulnerable to the ambitions of U.S. and Japanese multinationals.

What can European firms do to cope with the onslaught of U.S. and Japanese multinationals? Large European firms can

²⁸“From Guatemala with Love,” *Chain Leader*, September/October 2005, pp. 28–32.

counter U.S. competitors by exporting or investing directly in the United States and other markets. Red Bull, the Austrian company that created the energy drink category, expanded throughout Europe after the Maastricht Treaty came into force in 1993. In 1997 it was big enough to take on the American market and by 1999 its sales were \$75 million. Today, Red Bull is popular around the world. In 2006, more than 3 billion cans were sold in over 130 countries. And in 2007, the company sales amounted to 3.08 billion euro. On March 24, 2008 Red Bull introduced its first foray into the cola market

Source: Lance Eliot Brouters and Timothy J. Wilkinson, “Is the EU Destroying European Competitiveness?”, *Business Horizons*, 45 (July–August 2002), 37–42; *EU Foreign Direct Investment Yearbook 2007*, Luxembourg: Office for Official Publications of the European Communities, 2007; “Buyers Bullish on Red Bull, Sales Up,” *New Europe*, February 25, 2008, Issue 770, <http://www.neurope.eu/articles/83145.php>, accessed July 20, 2009; and “United Europe Celebrates Ethnic Diversity,” *CNN.com*, November 20, 2008.

with a product named “Simply Cola.” Mergers and acquisitions resulting from unification, also enhance the ability of EU firms to enter the United States. For example, in June of 2000 the French firm Publicis Group acquired Saatchi & Saatchi, the U.K.-based advertising firm, as a means of strengthening its position in the American market.

Smaller European firms are likely to consider pursuing a universal niche-market strategy. For instance, Iona Technologies, PLC, an Irish software firm, has successfully internationalized by pursuing a global niche-market strategy.

Finally, there remain EU customers who continue to prefer the more expensive, high-quality European products. Keeping this market segment from erosion by U.S. and Japanese competitors is key in retaining the viability of the EU market. The irony is that, if the failure of the EU Constitution is just the first event in a cascade of reversals for the integrationists, the newly refragmented markets may once again play a major role in strengthening the competitive position of smaller European firms.

The United States, which enjoys one of the highest per-capita income levels in the world, has long been the most important single market for both foreign and domestic companies. As a result of its insatiable demand for foreign products, the United States has been running a trade deficit since 1973—for three consecutive decades (more on this in Chapter 2). In the popular press, the trade deficits have often been portrayed as a declining competitiveness of the United States. This assumes—rather erroneously—that U.S. companies engaged only in exports and imports and that international trade takes place between independent buyers and sellers across national boundaries. In order to appreciate the complexities of global competition, the nature of international trade and international business must first be clarified, followed by a discussion of who manages international trade.

First of all, we have to understand the distinction between international trade and international business. Indeed, **international trade** consists of exports and imports, say, between the United States and the rest of the world. If U.S. imports exceed U.S. exports, then the nation would register a trade deficit. If the opposite were the case, then the United States would register a trade surplus. On the other hand, **international business** is a broader concept and includes international trade and foreign production. U.S. companies typically market their products in three ways. First, they can export their products from the United States, which is recorded as a U.S. export. Second, they can invest in their foreign production on their own and manufacture those products abroad for sale there. This transaction does not show up as a U.S. export. And third, they can contract out manufacturing in whole or part to a company in a foreign country, either by way of licensing or joint venture agreement. Of course, not all companies engage in all three forms of international transaction. Nonetheless, foreign manufacture, independently or contractually, is a viable alternative means to exporting products abroad. Although it is not widely known, foreign production constitutes a much larger portion of international business than international trade.

The extensive international penetration of U.S. and other companies has been referred to as *global reach*.²⁹ Since the mid-1960s, U.S.-owned subsidiaries located around the world have produced and sold three times the value of all U.S. exports. Although more recent statistics are not available, this 3:1 ratio of foreign manufacture to international trade had remained largely unchanged in the 1980 and 1990s, and it becomes much more conspicuous if we look at U.S. business with the European Union,

International Trade versus International Business

²⁹Richard J. Barnet and R. E. Muller, *Global Reach: The Power of the Multinational Corporations* (New York: Simon and Schuster, 1974).



Charles Thatcher/Tony Stone Images New York, Inc.

A Global Reach: Executives increasingly use a global map to visualize their strategy.

where U.S.-owned subsidiaries sold more than six times the total U.S. exports in 1990. Similarly, European-owned subsidiaries operating in the United States sold five times as much as U.S. imports from Europe.³⁰ This suggests that experienced companies tend to manufacture overseas much more than they export. On the other hand, Japanese companies did not expand their foreign manufacturing activities in earnest until about twenty years ago. According to one estimate, more than 90 percent of all the cases of Japanese FDI have taken place since 1985.³¹ Despite their relative inexperience in international expansion, Japanese subsidiaries registered two-and-a-half times as much foreign sales as all Japanese exports worldwide by 1990.³²

Who Manages International Trade?

As just discussed, international trade and foreign production are increasingly managed on a global basis. Furthermore, international trade and foreign production are also intertwined in a complex manner. Think about Honda Motors, a Japanese automobile manufacturer. Honda initially exported its Accords and Civics to the United States in the 1970s. By mid-1980s the Japanese company began manufacturing those cars in the United States in Marysville, Ohio. The company currently exports U.S.-made Accord models to Japan and elsewhere and boasts that it is the largest exporter of U.S.-made automobiles in the United States. Recently, Honda announced that it would start manufacturing its “world car” in Thailand, Brazil, and probably China, due to the low cost, and then export it mainly to Europe and Japan. It is expected that eventually all Honda cars in Japan will be produced and imported from abroad.³³ Similarly, Texas Instruments has a large semiconductor manufacturing plant in Japan, marketing its semiconductor chips not only in Japan but also exporting them from Japan to the United States and elsewhere. In addition to traditional exporting from their home base, these companies manufacture their products in various foreign countries both for local sale and for further exporting to the rest of the world, including their respective home countries. In other words, multinational companies (MNCs) are increasingly managing the international trade flow from within. This phenomenon is called **intra-firm trade**.

Intra-firm trade makes trade statistics more complex to interpret, since part of the international flow of products and components is taking place between affiliated companies

³⁰Peter J. Buckley and R. D. Pearce, “Overseas Production and Exporting by the World’s Largest Enterprises,” *International Executive*, 22 (Winter), 1980, pp. 7–8; Dennis J. Encarnation, “Transforming Trade and Investment, American, European, and Japanese Multinationals Across the Triad,” a paper presented at the Academy of International Business Annual Meetings, November 22, 1992.

³¹Masaaki Kotabe, “The Promotional Roles of the State Government and Japanese Manufacturing Direct Investment in the United States,” *Journal of Business Research*, 27 (June 1993), pp. 131–46.

³²Encarnation.

³³“Honda to Re-Import ‘World Car’ Produced in Thailand,” *Nikkei Interactive Net*, www.nni.nikkei.co.jp, December 18, 2001; “Honda Could Bring a Small Car to Europe from Thailand,” *Automotive News Europe*, December 13, 2004, p. 3.

within the same corporate system, transcending national boundaries. Although statistical information is scarce, one United Nations official report shows that in 1999, 34 percent of world trade was intra-firm trade between MNCs and their foreign affiliates and among those affiliates, and that additional 33.3 percent of world trade constituted exports by those MNCs and their affiliates. In other words, two-thirds of world trade is managed one way or another by MNCs.³⁴ These trade ratios have been fairly stable over time.³⁵

Although few statistics are available, service industries are going through the same evolution as manufacturing industries on a global basis. Indeed, some similarities exist in intra-firm trade of services. In 2007 alone, world commercial services exports rose by 18 percent to \$3.3 trillion. Among the top global service exporters and importers, the United States was still ranked the largest exporter, providing \$454 billion of services to the rest of the world. The United States was also the top importer of services, receiving \$440 billion worth of services.³⁶ As stated earlier in the chapter, however, the severe global recession is expected to reduce the global trade for the first time in over 25 years.³⁷ Today, approximately 16 percent of the total value of U.S. exports and imports of services were conducted across national boundaries on an intra-firm basis.³⁸ Government deregulation and technological advancement have facilitated the tradability of some services globally and economically.

EVOLUTION OF GLOBAL MARKETING



Marketing is essentially the activity, set of institutions, and processes for creating, communicating, delivering, and exchanging offerings that have value for customers, clients, partners, and society at large.³⁹ Marketing is not only much broader than selling, it also encompasses the entire company's *market orientation* toward customer satisfaction in a competitive environment. In other words, marketing strategy requires close attention to both customers and competitors.⁴⁰ Quite often marketers have focused excessively on satisfying customer needs while ignoring competitors. In the process, competitors have outmaneuvered them in the marketplace with better, less-expensive products. It is widely believed that in many cases, U.S. companies have won the battle of discovering and filling customer needs initially, only to be defeated in the competitive war by losing the markets they pioneered to European and Japanese competitors.⁴¹

What Is Marketing?

³⁴Khalil Hamdani, "The Role of Foreign Direct Investment in Export Strategy," presented at 1999 Executive Forum on National Export Strategies, International Trade Centre, the United Nations, September 26–28, 1999.

³⁵United Nations Center on Transnational Corporations, *Transnational Corporations in World Development: Trends and Perspectives*, New York: United Nations, 1988; Organization for Economic Cooperation and Development, *Intra-Firm Trade*, Paris, OECD, 1993; William J. Zeile, "U.S. Affiliates of Foreign Companies," *Survey of Current Business*, August 2005, pp. 198–214.

³⁶*World Trade Report 2008*, Geneva, World Trade Organization, www.wto.org, 2008.

³⁷World Bank, *Global Economic Prospect 2009*, www.worldbank.org/gep2009.

³⁸Janet Y. Murray and Masaaki Kotabe, "Sourcing Strategies of U.S. Service Companies: A Modified Transaction-Cost Analysis," *Strategic Management Journal*, 20, September 1999, 791–809; Masaaki Kotabe and Janet Y. Murray, "Global Procurement of Service Activities by Service Firms," *International Marketing Review*, 21 (6), 2004, 615–633; for detailed statistics, see Michael A. Mann, Laura L. Brokenbaugh, Sylvia E. Bargas, "U.S. International Services," *Survey of Current Business*, 80, October 2000, pp. 119–61.

³⁹This is the definition of marketing adopted by the American Marketing Association in October 2007, and is strongly influenced by Drucker's conception of two entrepreneurial functions—marketing and innovation—that constitute business. Recent thinking about marketing also suggests the task of the marketer is not only to satisfy the current needs and wants of customers, but also to innovate on products and services, anticipating and even creating their future needs and wants. See Peter F. Drucker, *The Practice of Management* (New York: Harper & Brothers, 1954), pp. 37–39; and also Frederick E. Webster, Jr., "The Changing Role of Marketing in the Corporation," *Journal of Marketing*, 56 (October 1992), pp. 1–16.

⁴⁰Aysegül Özsomer and Bernard Simonin, "Antecedents and Consequences of Market Orientation in a Subsidiary Context," *Enhancing Knowledge Development in Marketing*, 1999 American Marketing Association Educators' Proceedings, Summer 1999, p. 68.

⁴¹Robert M. Peterson, Clay Dibrell, and Timothy L. Pett, "Whose Market Orientation is Longest: A Study of Japan, Europe, and the United States," *Enhancing Knowledge Development in Marketing*, 1999 American Marketing Association Educators' Proceedings, Summer 1999, p. 69.

It is increasingly difficult for companies to avoid the impact of competition from around the world and the convergence of the world's markets. As a result, an increasing number of companies are drawn into marketing activities outside their home country. However, as previously indicated, different companies approach marketing around the world very differently. For example, Michael Dell established Dell Computer because he saw a burgeoning market potential for IBM-compatible personal computers in the United States. After his immediate success at home, he realized a future growth potential would exist in foreign markets. Then his company began exporting Dell PCs to Europe and Japan. In a way this was a predictable pattern of foreign expansion. On the other hand, not all companies go through this predictable pattern. Think about a notebook-sized Macintosh computer called the PowerBook 100 that Apple Computer introduced in 1991. In 1989, Apple enlisted Sony, the Japanese consumer electronics giant, to design and manufacture this notebook computer for both the U.S. and Japanese markets.⁴² Sony has world-class expertise in miniaturization and has been a supplier of disk drives, monitors, and power supplies to Apple for various Macintosh models. In an industry such as personal computers, where technology changes quickly and the existing product becomes obsolete in a short period of time, a window of business opportunity is naturally limited. Therefore, Apple's motivation was to introduce the notebook computer on the markets around the world as soon as it could before competition picked up.

Companies generally develop different marketing strategies depending on the degree of experience and the nature of operations in international markets. Companies tend to evolve over time, accumulating international business experience and learning the advantages and disadvantages associated with complexities of manufacturing and marketing around the world.⁴³ As a result, many researchers have adopted an evolutionary perspective of internationalization of the company just like the evolution of the species over time. In the following pages we will formally define and explain five stages that characterize the evolution of global marketing. Of course, not all companies go through the complete evolution from a purely domestic marketing stage to a purely global marketing stage. An actual evolution depends also on the economic, cultural, political, and legal environments of various country markets in which the company operates, as well as on the nature of the company's offerings. A key point here is that many companies are constantly under competitive pressure to move forward both *reactively* (responding to the changes in the market and competitive environments) and *proactively* (anticipating the change). Remember, "if you stand still, you will get run over."

Therefore, knowing the dynamics of the evolutionary development of international marketing involvement is important for two reasons. First, it helps in the understanding of how companies learn and acquire international experience and how they use it for gaining competitive advantage over time. This may help an executive better prepare for the likely change needed in the company's marketing strategy. Second, with this knowledge, a company may be able to compete more effectively by predicting its competitors' likely marketing strategy in advance.

As shown in **Exhibit 1.2**, there are five identifiable stages in the evolution of marketing across national boundaries.⁴⁴ These evolutionary stages are explained below.

Domestic Marketing

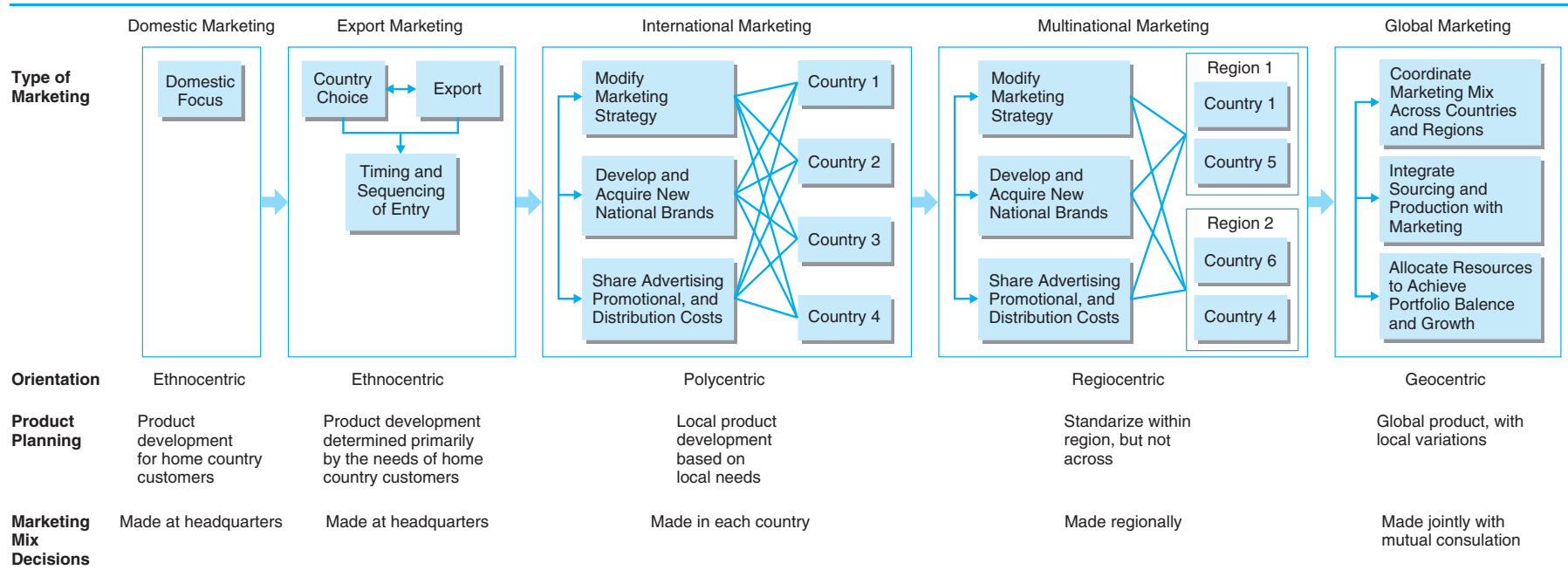
The first stage is **domestic marketing**. Before entry into international markets, many companies focus solely on their domestic market. Their marketing strategy is developed based on information about domestic customer needs and wants, industry trends,

⁴²"Apple's Japanese Ally," *Fortune* (November 4, 1991), pp. 151–52.

⁴³Anna Shaojie Cui, David A. Griffith, S. Tamer Cavusgil, "The Influence of Competitive Intensity and Market Dynamism on Knowledge Management Capabilities of Multinational Corporation Subsidiaries," *Journal of International Marketing*, 13 (3), 2005, pp. 32–53).

⁴⁴This section draws from Balaj S. Chakravarthy and Howard V. Perlmutter, "Strategic Planning for A Global Business," *Columbia Journal of World Business* (Summer 1985), pp. 3–10; Susan P. Douglas and C. Samuel Craig, "Evolution of Global Marketing Strategy: Scale, Scope and Synergy," *Columbia Journal of World Business* 24 (Fall 1989), pp. 47–59.

EXHIBIT 1-2
EVOLUTION OF GLOBAL MARKETING



Sources: Constructed from Susan P. Douglas and C. Samuel Craig, "Evolution of Global Marketing Strategy: Scale, Scope and Synergy," Columbia Journal of World Business, 24 (Fall 1985), p. 50; and Balaji S. Chakravarty and Howard V. Perlmutter, "Strategic Planning for a Global Business," Columbia Journal of World Business, 20 (Summer 1985), p. 6.

economic, technological, and political environments at home. When those companies consider competition, they essentially look at domestic competition. Today, it is highly conceivable that competition in a company's home market is made up of both domestic competitors and foreign competitors marketing their products in the home market. Domestic marketers tend to be *ethnocentric* and pay little attention to changes taking place in the global marketplace, such as changing lifestyles and market segments, emerging competition, and better products that have yet to arrive in their domestic market. *Ethnocentrism* is defined here as a predisposition of a firm to be predominantly concerned with its viability worldwide and legitimacy only in its home country⁴⁵—that is, where all strategic actions of a company are tailored to domestic responses under similar situations. As a result, they may be vulnerable to the sudden changes forced on them by foreign competition. For example, U.S. automakers suffered from this ethnocentrism in the 1960s and 1970s as a result of their neglect of imminent competition from Japanese automakers with more fuel-efficient cars that would eventually seize a market opportunity in the United States as a result of the two major oil crises in the 1970s.

Export Marketing

The second stage is **export marketing**. Usually, export marketing begins with unsolicited orders from foreign customers. When a company receives an order from abroad, initially it may fill it reluctantly, but it gradually learns the benefit of marketing overseas. In general, in the early stage of export marketing involvement, the internationalization process is a consequence of incremental adjustments to the changing conditions of the company and its environment, rather than a result of its deliberate strategy. Such a pattern is due to the consequence of greater uncertainty in international business, higher costs of information, and the lack of technical knowledge about international marketing activities. At this early export marketing stage, exporters tend to engage in *indirect exporting* by relying on export management companies or trading companies to handle their export business.

Some companies progress to a more involved stage of internationalization by *direct exporting*, once three internal conditions are satisfied. First, the management of the company obtains favorable expectations of the attractiveness of exporting based on experience. Second, the company has access to key resources necessary for undertaking additional export-related tasks. Such availability of physical, financial, and managerial resources is closely associated with firm size. Particularly small companies may have few trained managers and little time for long-term planning, as they are preoccupied with day-to-day operational problems; consequently, they find it difficult to become involved in exporting. Third, management is willing to commit adequate resources to export activities.⁴⁶ The company's long-term commitment to export marketing depends on how successful management is in overcoming various barriers encountered in international marketing activities. An experienced export marketer has to deal with difficulties in maintaining and expanding export involvement. These difficulties include import/export restrictions, cost and availability of shipping, exchange rate fluctuations, collection of money, and development of distribution channels, among others. Overall, favorable experience appears to be a key component in getting companies involved in managing exports directly without relying on specialized outside export handlers. To a large degree an appropriate measure of favorableness for many companies consists of profits. An increase in profits due to a certain activity is likely to increase the company's interest in such activity.⁴⁷

External pressures also prod companies into export marketing activities. Saturated domestic markets may make it difficult for a company to maintain sales volume in an

⁴⁵Chakravarthy and Perlmutter, pp. 3–10.

⁴⁶S. Tamer Cavusgil, "On the Internationalization Process of Firms," *European Research*, 8 (November 1980), pp. 273–79.

⁴⁷Masaaki Kotabe and Michael R. Czinkota, "State Government Promotion of Manufacturing Exports: A Gap Analysis," *Journal of International Business Studies*, 23 (Fourth Quarter 1992), pp. 637–58.

increasingly competitive domestic market; it will become much more serious when foreign competitors begin marketing products in the domestic market. Export marketers begin paying attention to technological and other changes in the global marketplace that domestic marketers tend to ignore. However, export marketers still tend to take an ethnocentric approach to foreign markets as being an extension of their domestic market and export products developed primarily for home country customers with limited adaptation to foreign customers' needs.

Once export marketing becomes an integral part of the company's marketing activity, it will begin to seek new directions for growth and expansion. We call this stage **international marketing**. A unique feature of international marketing is its *polycentric* orientation with emphasis on product and promotional adaptation in foreign markets, whenever necessary.⁴⁸ Polycentric orientation refers to a predisposition of a firm to the existence of significant local cultural differences across markets, necessitating the operation in each country being viewed independently (i.e., all strategic decisions are thus tailored to suit the cultures of the concerned country). As the company's market share in a number of countries reaches a certain point, it becomes important for the company to defend its position through local competition. Because of local competitors' proximity to, and familiarity with, local customers, they tend to have an inherent "insider" advantage over foreign competition. To strengthen its competitive position, the international marketer could adapt its strategy, if necessary, to meet the needs and wants of local customers in two alternative ways. First, the company may allocate a certain portion of its manufacturing capacity to its export business. Second, because of transportation costs, tariffs, and other regulations, and availability of human and capital resources in the foreign markets, the company may even begin manufacturing locally. BMW has been exporting its cars to the United States for many years. In 1992, the German company invested in a manufacturing plant in South Carolina in order to be more adaptive to changing customer needs in this important market, and to take advantage of rather inexpensive resources as a result of the dollar depreciation against the euro. Accordingly, BMW South Carolina has become part of BMW Group's global manufacturing network and is the exclusive manufacturing plant for all Z4 roadster and X5 Sports Activity Vehicles.⁴⁹

If international marketing is taken to the extreme, a company may establish an independent foreign subsidiary in each and every foreign market and have each of the subsidiaries operate independently of each other without any measurable headquarters control. This special case of international marketing is known as **multidomestic marketing**. Product development, manufacturing, and marketing are all executed by each subsidiary for its own local market. As a result, different product lines, product positioning, and pricing may be observed across those subsidiaries. Few economies of scale benefits can be obtained. However, multidomestic marketing is useful when customer needs are so different across different national markets that no common product or promotional strategy can be developed. Even Coca-Cola, which used to practice globally standardized marketing strategy, changed its strategy when it found that its structure had become too cumbersome and that it was insensitive to local markets. In 2000, the company decided to return to a more multidomestic marketing approach and to give more freedom to local subsidiaries. Local marketing teams are now permitted to develop advertising to local consumers and even launch new local brands.⁵⁰

At this stage, the company markets its products in many countries around the world. We call this stage **multinational marketing**. Management of the company comes to realize the benefit of economies of scale in product development, manufacturing, and marketing by consolidating some of its activities on a regional basis. This *regiocentric* approach suggests

International Marketing

Multinational Marketing

⁴⁸Warren J. Keegan, "Multinational Product Planning: Strategic Alternatives," *Journal of Marketing*, 33 (January 1969), pp. 58–62.

⁴⁹<http://www.bmwusa.com/about/>, accessed January 27, 2006.

⁵⁰Isabelle Schuiling and Jean-Noël Kapferer, "Real Differences between Local and International Brands: Strategic Implications for International Marketers," *Journal of International Marketing*, 12 (4), 2004, pp. 97–112.

that product planning may be standardized within a region (e.g., a group of contiguous and similar countries), such as Western Europe, but not across regions. Products may be manufactured regionally as well. Similarly, advertising, promotion, and distribution costs may also be shared by subsidiaries in the region. In order for the company to develop its regional image in the marketplace, it may develop and acquire new regional brands to beef up its regional operations. Caterpillar now has a regional headquarters in Europe that has united and integrated its geographically diverse organizations, and a unique joint venture with Mitsubishi Heavy Industries to meet the exacting Japanese quality standards for the Japanese market and beyond.

Global Marketing

The international (country-by-country) or multinational (region-by-region) orientation, while enabling the consolidation of operations within countries or regions, will tend to result in market fragmentation worldwide, nonetheless. Operational fragmentation leads to higher costs. When many Japanese companies entered the world markets as low-cost manufacturers of reliable products in the 1970s, well-established U.S. and European multinational companies were made acutely aware of their vulnerability as high-cost manufacturers. Levitt,⁵¹ an arduous globalization proponent, argues:

Gone are accustomed differences in national or regional preference. Gone are the days when a company could sell last year's models—or lesser versions of advanced products—in the less developed world. . . . The multinational and the global corporation are not the same thing. The multinational corporation operates in a number of countries, and adjusts its products and practices in each—at high relative costs. The global corporation operates with resolute constancy—at low relative cost—as if the entire world (or major regions of it) were a single entity; it sells the same things in the same way everywhere.

Global marketing refers to marketing activities by companies that emphasize the following:

1. *Standardization efforts*—standardizing marketing programs across different countries particularly with respect to product offering, promotional mix, price, and channel structure. Such efforts increase opportunities for the transfer of products, brands, and other ideas across subsidiaries and help address the emergence of global customers
2. *Coordination across markets*—reducing cost inefficiencies and duplication of efforts among their national and regional subsidiaries
3. *Global Integration*—participating in many major world markets to gain competitive leverage and effective integration of the firm's competitive campaigns across these markets by being able to subsidize operations in some markets with resources generated in others and responding to competitive attacks in one market by counterattacking in others.⁵²

Although Levitt's view is somewhat extreme, many researchers agree that global marketing does not necessarily mean standardization of products, promotion, pricing, and distribution worldwide, but rather it is a company's proactive willingness to adopt a global perspective instead of country-by-country or region-by-region perspective in developing a marketing strategy. Clearly, not all companies adopt global marketing. Yet an increasing number of companies are proactively trying to find commonalities in their marketing strategy among national subsidiaries (see **Global Perspective 1-3**). For example, Black & Decker, a U.S. manufacturer of hand tools, adopted a global perspective by standardizing and streamlining components such as motors and rotors while maintaining a wide range of product lines, and created a universal image for its products. In this case, it was not standardization of products per se but rather the company's effort at standardizing key components and product design for manufacturability in the manufacturing industry and core, supplementary services in the service

⁵¹Theodore Levitt, "The Globalization of Markets," *Harvard Business Review*, 61 (May–June) 1983, pp. 92–102.

⁵²Shaoming Zou and S. Tamer Cavusgil, "The GMS: A Broad Conceptualization of Global Marketing Strategy and Its Effect on Firm Performance," *Journal of Marketing*, 66, October 2002, pp. 40–56.



GLOBAL PERSPECTIVE 1-3

GLOBALIZING THE BUSINESS TERMS BEFORE GLOBALIZING THE FIRM

International was the first word that William Hudson, president and CEO of AMP Inc., Harrisburg, Pennsylvania, told his corporate colleagues to cut from their business vocabularies. Why? The term creates a “Chinese wall” that divides a globalizing company into “domestic” and “international” sides, he explained to A. T. Kearney Inc. officers meeting in Chicago. “It’s almost as if you don’t jump over that wall” to work or team together, he said.

Another banished word: “subsidiary.” It conveys “a parent/child relationship,” said Mr. Hudson. Headquarters tends to lord its power over foreign and domestic operations and “make them feel like inferior souls.” Revising the business lexicon is not easy, Mr. Hudson readily admitted. “Every now and then [one of the words] shows up on a . . . slide when

Sources: Jon Erlendsson, “Globalization and Innovation,” http://www.hi.is/~joner/eaps/cq_globi.htm, accessed December 15, 2005; and Herman E. Daly, “Globalization versus Internationalization: Some Implications,” <http://www.globalpolicy.org/globaliz/econ/herman2.htm>, accessed August 10, 2008.

somebody makes a presentation. And I’ve got to put up my hand and say: ‘Erase that word.’”

Next, what is the difference between internationalization and globalization? According to Herman E. Daly, “Internationalization refers to the increasing importance of international trade, international relations, treaties, alliances, etc. Inter-national, of course, means between or among nations. The basic unit remains the nation, even as relations among nations become increasingly necessary and important. Globalization refers to global economic integration of many formerly national economies into one global economy, mainly by free trade and free capital mobility, but also by easy or uncontrolled migration. It is the effective erasure of national boundaries for economic purposes . . .” Briefly speaking, the key difference between internationalization and globalization lies in that internationalization takes place between individual nations, between individual companies operating in different countries, and between individual citizens of different countries; globalization, however, increasingly ignores national boundaries.

industry, to achieve global leadership in cost and value across common market segments around the world.

Global marketing does not necessarily mean that products can be developed anywhere on a global basis. The economic geography, climate, and culture, among other things, affect the way in which companies develop certain products and consumers want them. First, the availability of resources is a major determinant of industry location. The U.S. automobile industry was born at the dawn of the twentieth century as a result of Henry Ford having decided to locate his steel-making foundry in Detroit midway between sources of iron ore in the Mesabi range in Minnesota and sources of bituminous coal in Pennsylvania. Similarly, in the last quarter of the twentieth century, Silicon Valley, in and around Palo Alto, California and Silicon Hill, in Austin, Texas, emerged as high-tech Meccas as a result of abundant skilled human resources (thanks to leading universities in the areas), aided by warm, carefree environments—a coveted atmosphere conducive to creative thinking. For the same reason, Bangalore in India has emerged as an important location for software development. Brazil boasts that more than half of the automobiles on the road run on a hundred percent pure alcohol, thanks to an abundant supply of ethanol produced from subsidized sugar cane. Even bananas are produced in abundance in Iceland, thanks to nature-provided geothermal energy tapped in greenhouses.⁵³ Since Germans consume the largest amount of bananas, about 33 lbs (or 15 kg) on a per capita basis, in the European Union, Iceland could become an exporter of bananas to Germany!⁵⁴

Obviously, the availability of both natural and human resources is important in primarily determining industry location as those resources, if unavailable, could become a bottleneck. It is to be stressed that consumer needs are equally important

The Impact of Economic Geography and Climate on Global Marketing

⁵³“Iceland Information,” http://www.vjv.com/information/country/europe_west/iceland_info.html, accessed December 15, 2005.

⁵⁴Paul Sutton, “The Banana Regime of the European Union, the Caribbean, and Latin America,” *Journal of Interamerican Studies and World Affairs*, 39, Summer 1997, pp. 5–36.

as a determinant of industry location.⁵⁵ As the Icelandic banana example shows, the fact that Germans consume a large amount of bananas gives Icelandic growers a logistical advantage. Ask yourself why cellular phones have been most widely adopted in Finland, and why fax machines and ink-jet printers have been most widely developed in Japan. In Finland and other Scandinavian countries, it snows heavily in winter but it is very damp snow owing to the warm Gulf Stream moderating what could otherwise be a frigid climate. The damp snow frequently cuts off power lines. Thus, Scandinavians always wished for wireless means of communication, such as CB radios and cellular phones. Companies such as Nokia in Finland and Ericsson in Sweden have become world-class suppliers of cellular technology.⁵⁶ Similarly, Japanese consumers always wanted machines that could easily produce and reproduce the complex characters in their language. Thus, Japanese companies such as Canon, Epson (a subsidiary of Seiko Watch), and Fujitsu have emerged as major producers of fax and ink-jet printers in the world. For outdoor activity-loving Australians, surfing is a national sport. No wonder that Quiksilver, an Australian company that knows quite well how to design sports-wear that is functional as well as aesthetic, has conquered the European market from skateboarders beneath the Eiffel Tower to snowboarders in the Swiss Alps and surfers in Spain.⁵⁷ Similarly, Billabong, another Australian surfing goods retailer with a keen eye for what outdoor sports lovers want to wear, is expanding into the U.S. market with a broad range of leisure-related products following the acquisition of Element, a U.S. skateboarding clothing company, and Von Zipper, a U.S. sunglasses and snow goggles brand.⁵⁸ Indeed, as the old proverb says, “necessity is the mother of invention.”

The point is that what companies can offer competitively may be determined either by the availability of natural and human resources or by the unique consumer needs in different countries or regions or by both. Global marketers are willing to exploit their local advantages for global business opportunities. Then ask yourself another question about an emerging societal need around the world: environmental protection. Where are formidable competitors likely to originate in the near future? We think it is Germany. Germans have long been concerned about their environmental quality as represented by the cleanliness of the Rhine River. When phosphorus—a major whitening agent in laundry detergent, polluted the Rhine —, the German government was the first in the world to ban its use. Now German companies are keen on developing products that are fully recyclable. In a not too distant future recyclable products will become increasingly important. Naturally, marketing executives need to have an acute understanding of not only the availability of various resources but also emerging consumer and societal needs on a global basis.

So far we focused on complex realities of international trade and investment that have characterized our global economy in the past twenty years. Some vital statistics have been provided. The more statistics we see, the more befuddled we become by the sheer complexities of our global economy. It even seems as though there were not a modicum of orderliness in our global economy, it being just like a jungle. Naturally, we wish the world had been much simpler. In reality, it is becoming ever more complex. Luckily enough, however, economists and business researchers have tried over the years to explain the ever-increasing complexities of the global economy in simpler terms. A simplified yet logical view of the world is called a **theory**. Indeed, there are many different ways—theories—of looking at international trade and investment taking place in the world. For those of you interested in understanding some orderliness in the complex world of international trade and investment, we encourage you to read the appendix to this chapter. Some theoretical understanding will not only help you appreciate the competitive world in which we live, but also help you make better strategy decisions for a company you may join shortly or a company you may own.

⁵⁵Michael E. Porter, *The Competitive Advantage of Nations*, New York: Free Press, 1990.

⁵⁶Lilach Nachum, “Does Nationality of Ownership Make Any Difference and If so Under What Circumstances,” *Journal of International Management*, 9, 2003.

⁵⁷“Global Surfin’ Safari: Quiksilver Rides Wave In Europe and Far East,” *Women’s Wear Daily*, June 30, 2005, pp. 1–8.

⁵⁸“Skateboarding Springs into Billabong,” *The Australian*, July 4, 2001, p. 21.

SUMMARY

World trade has grown from \$200 billion to more than \$17 trillion in the last 30 years, although the current global recession is expected to reduce world trade for the first time in over 25 years. Although world trade volume is significant in and of itself, international business is much bigger than trade statistics show. Companies from Western Europe, the United States, and Japan collectively produce probably more than three times as much in their foreign markets than they export. And about a third of their exports and imports are transacted on an intra-firm basis between their parent companies and their affiliated companies abroad or between the affiliated companies themselves.

What this all means is that it is almost impossible for domestic company executives to consider their domestic markets and domestic competition alone. If they fail to look beyond their national boundaries, they may unknowingly lose marketing opportunities to competitors that do. Worse yet, foreign competitors will encroach on their hard-earned market position at home so fast that it may be too late for them to respond. International markets are so intertwined that separating international from domestic business may be a futile mental exercise.

Historically, international expansion has always been a strategy consideration after domestic marketing, and has therefore been reactionary to such things as a decline in domestic sales and increased domestic competition. Global marketing is a proactive response to the intertwined nature of business opportunities and competition that know no political boundaries. However, global marketing does not necessarily mean that companies should market the same product in the same way around the world as world markets are converging. To the extent feasible, they probably should. Nonetheless, global marketing is a company's willingness to adopt a global perspective instead of country-by-country or region-by-region perspective in developing a marketing strategy for growth and profit.

What companies can offer competitively may be determined either by the availability of natural and human resources or by the unique consumer needs in different countries or regions or by both. Global marketers should be willing to exploit their local advantages for global marketing opportunities. The proliferation of e-commerce on the Internet accelerates such global marketing opportunities.

KEY TERMS

Domestic marketing
Electronic commerce
(E-commerce)

Export marketing
Global marketing
International business

International marketing
International trade
Intra-firm trade

Multidomestic marketing
Multinational marketing
Triad regions

REVIEW QUESTIONS

1. Why is international business much more complex today than it was twenty years ago?
2. What is the nature of global competition?
3. Does international trade accurately reflect the nature of global competition?
4. Why are consumption patterns similar across industrialized countries despite cultural differences?
5. How is global marketing different from international marketing?
6. Why do you think a company should or should not market the same product in the same way around the world?
7. What is proactive standardization?
8. How is the Internet reshaping the nature of global marketing?

DISCUSSION QUESTIONS

1. The United States and Japan, the two largest economies in the world, are also the largest importers and exporters of goods and services. However, imports and exports put together comprise only 20 to 30 percent of their GDPs. This percentage has not changed much over the last three decades for both of these countries. Does this imply that the corporations and the media may be overemphasizing globalization? Discuss why you agree or do not agree with the last statement.
2. Merchandise trade today accounts for less than 2 percent of all the foreign exchange transactions around the world. Can one deduce that merchandise plays an insignificant role in today's economies? Why or why not?
3. A major cereal manufacturer produces and markets standardized breakfast cereals to countries around the world. Minor modifications in attributes, such as sweetness of the product, are made to cater to local needs. However, the core products and brands are standardized. The company entered the Chinese market a few years back and was extremely satisfied with the results. The company's sales continue to grow at a rate of around 50 percent a year in China.

Encouraged by its marketing success in China and other Asian countries, and based on the market reforms taking place, the company started operations in India by manufacturing and marketing its products. Initial response to the product was extremely encouraging and within one year the company was thinking in terms of rapidly expanding its production capacity. However, after a year, sales tapered off and started to fall. Detailed consumer research seemed to suggest that while the upper-middle social class, especially families where both spouses were working, to whom this product was targeted, adopted the cereals as an alternative meal (i.e., breakfast) for a short time, they eventually returned to the traditional Indian breakfast. The CEOs of some other firms in the food industry in India are quoted as saying that non-Indian snack products and the restaurant business are the areas where multinational companies (MNCs) can hope for success. Trying to replace a full meal with a non-Indian product has less of a chance of succeeding. You are a senior executive in the international division of this food MNC with experience of operating in various countries in a product management function. The CEO plans to send you to India on a fact-finding mission to determine answers to these specific questions. What, in your opinion, would be the answers:

- a. Was entering the market with a standardized product a mistake?
 - b. Was it a problem of the product or the way it was positioned?
 - c. Given the advantages to be gained through leveraging of brand equity and product knowledge on a global basis, and the disadvantages of differing local tastes, what would be your strategy for entering new markets?
4. Globalization involves the organization-wide development of a global perspective. This global perspective requires globally thinking managers. Although the benefits of globalization have received widespread attention, the difficulties in developing managers who think globally has received scant attention. Some senior managers consider this to be a significant stumbling block in the globalization efforts of companies. Do you agree with the concerns of these managers? Would the lack of truly globally thinking managers cause problems for implementing a global strategy? And how does the proliferation of e-commerce affect the way these managers conduct business?
 5. The e-commerce business in China has entered a golden period, with transaction volume of online trading reaching 21.86 billion yuan (US\$2.64 billion) in 2004. With 94 million Internet users, more than 40 million people conducted transactions on the Internet in 2004, compared with 10.7 million in 2001, and more than 60 percent of people expressed their willingness to try online trading in 2005. Among net citizens, roughly 20 million people have had the experience of playing games online. China's largest e-game operator, Shanda Interactive Entertainment Limited has accumulated a huge amount of wealth in just a couple of years. In May 2004, Shanda was listed on the NASDAQ and generated US\$373 million in the online games market; 39.3 percent of this market is from China. Now the company is shifting its business focus from the computer platform to the TV platform—including games, music and literature—through a set-top box to penetrate those 340 million households that already own a television. With 1.3 billion in population, the Chinese market is inviting to both online and offline businesses. In terms of online businesses, what do you foresee as opportunities and threats to multinational corporations, especially in emerging economies?

SHORT CASES

CASE 1-1

GLOBAL MARKETING REQUIRES A VERY LOCAL ATTENTION: A LESSON FROM VODAFONE'S LOSS OF JAPAN UNIT



As the world's leading mobile telecommunications company, Vodafone Group, a British company, has a significant presence in Europe, the Middle East, Africa, Asia Pacific, and the United States through the Company's subsidiary undertakings, joint ventures, associated undertakings and investments. According to the latest data, the Company had a total market capitalization of approximately £99 billion on December 31 2007. However, the company's road to success is not always smooth. Vodafone's five years of struggle in Japan from 2001 until its final sale of the unit in March 2006, proves that global marketing does not necessarily mean that a global company can treat all markets the same way. In essence, think globally, but act locally.

Since entering the Japanese market in 2001 by taking over J-Phone Co., a local cellular provider, the company had seen its reputation slip with its handsets being viewed dull and its service second rate. Vodafone was focused on building a global brand and cutting costs by producing large numbers of handsets to sell throughout the world. In Japan, however, this came at the expense of products and services to suit the nation's finicky and tech-savvy consumers. In July 2004, Vodafone's unit in Japan, Vodafone KK, became the first of the three carriers to report a monthly net loss of customers from the period one year earlier. Four years after its entry into Japan, Vodafone ended up being slower than Japanese rivals to roll out flashy new handsets and competitive price plans. It failed to gain market share, far lagging behind two other of Japan's major cellular carriers, NTT DoCoMo and KDDT. The two winners simply out-hustled Vodafone by coming up with cooler designs and must-have services. AU attracted plenty of buzz with a high-speed music download service, for instance. Vodafone's struggle in Japan shows that it is not always an advantage to act like a big global player.

Sources: Ian Rowley, "Vodafone's Bad Connection In Japan," *BusinessWeek.com*, February 21, 2005; Ian Rowley, "Can Vodafone Get Through?" *BusinessWeek.com*, February 28, 2006; and Kerry Capell, "Vodafone's Tough Calls," *BusinessWeek.com*, February 28, 2006 (4). Ian Rowley and Kenji Hall, "Softbank-Vodafone Deal Rings True," *BusinessWeek.com*, March 17.

For a long time, Vodafone KK had been accustomed to getting management directives from its London headquarters. After its steady decline in Japan from 2001 to 2005, Vodafone's Japanese unit realized that more ideas should have originated in Japan, instead of trying hard to make European handsets fly in the Japanese market. In early 2005, Vodafone dispatched Bill Morrow to Tokyo to run its Japan operations with a largely modified marketing strategy. There were signs that Vodafone did make some headway in Japan since then with its transition from 2G to 3G, a greater range of new tailored handsets and services, much better content and a stronger network, as can be reflected by numbers: In January, 2005, Vodafone lost 59,000 subscribers on a net basis, an alarming figure. One year after, by comparison, it pulled in 17,600, after signing up 63,700 subscribers in December 2005. That pushed total subscribers above the 15.1 million mark.

However, reviving in Japan was not easy after a long-time loss largely due to lack of local attention. The worst thing was that time was running out. In spite of its endeavor to recover its Japan market, by early 2006, Vodafone was still far behind its rivals with its market share of 16.7 percent compared to 24.1 percent for KDDI's AU brand and 55.8 percent for DoCoMo.

As a closure, on March 17, 2006, Vodafone sold its 97.7 percent holding in Vodafone Japan to SoftBank, which had planned to get into cellular in 2007, for \$15.5 billion after the company had struggled to gain traction in Japan. With this deal Vodafone finally relieved its executives of the headache of trying to fix a unit with sinking profitability and little hope of catching bigger rivals NTT DoCoMo and KDDI unit AU.

DISCUSSION QUESTIONS

1. Why would a firm such as Vodafone need to have a global marketing strategy even though its product development, as well as the rest of its marketing strategy, needs to be localized for tech-savvy consumers in Japan?
2. What alternative strategy might Vodafone have used to set a strong market position in Japan from the very beginning?
3. What implications can you draw from Vodafone's loss of its Japan unit with regard to global firms' tapping into the convergence among global consumers?



ASE 1-2

KEEPING WITH THE TIMES—MCDONALD'S, I'M LOVIN' IT!

McDonald's, the world's largest restaurant chain with over 30,000 outlets in more than 115 countries, brings to mind many terms: golden arches, Big Macs, McNuggets, affordable meals, brand value, and American capitalism, to name just a few. How did McDonald's become one of the world's best-known brands? Needless to say, being in the food industry entails different menus for different parts of the world based on varying tastes and preferences. At the time, McDonald's made its foray into foreign markets it was almost impossible to have a mass marketing or global strategy in terms of McDonald's menu items. Therefore, the company adopted a strategy to appeal to those different preferences. According to the company, the secret to its successful brand is a type of multidomestic strategy, which the company used successfully by being able to offer different menus in different countries.

Previously, McDonald's even extended this strategy to marketing for its restaurants in foreign markets. Remember the yellow and red-garbed clown that attracted kids to McDonald's? McDonald's had maintained the same image for years and by the start of the twenty-first century, it was not working anymore. Additionally, the growing health consciousness among consumers the world over caused the restaurant chain to suffer decreasing profitability. Nevertheless, by 2005, the year that marked its fiftieth anniversary, McDonald's was on its way to regaining its stardom.

With time, it is necessary for companies to keep abreast of the changes that are taking place in the environment. Today, many firms are shifting from a multidomestic or multinational strategy to a more global one. It is believed that one reason for this is the growing convergence in consumer behavior, especially for food and apparel. For example, consumers all over the world are moving toward a healthy lifestyle that includes a healthy diet and exercise. For firms, a global strategy allows them to minimize overall costs, and specifically marketing costs, by repeating commercials with few alterations, justifying high advertising expenditure to release a perfect ad. McDonald's is one of several companies that have adopted a global

marketing strategy. McDonald's has had to revive its global business over the past five years, one of the ways to do it being to replace its previous shoddy image with a hip new one.

In the year 2003, the company launched its first truly global marketing campaign called "I'm lovin' it." The new promotion effort aimed at changing the company's image in markets all over the world sends the same message to its global consumers with small changes for local tastes and preferences. Thus, even though there is still a significant divergence in McDonald's menus, the new global marketing campaign instilled a distinct global brand value in the minds of consumers. McDonald's invested heavily in the campaign, employing celebrities, such as singer Justin Timberlake and popular music group Destiny's Child who draw a global audience, to appear in its advertisements. In addition, McDonald's introduced more healthy foods in its menus such as salads. The "I'm lovin' it" marketing campaign was targeted at consumers in all age groups from kids and young adults to seniors. The conceptualization of the ad was also global. It was the brainchild of a Germany-based firm Heye and Partner; the company settled on this agency after consulting with several marketing agencies in many different countries. The campaign has been one of the most successful of its time. The strategy worked, and in just one year, the company's revenues were up by more than 10 percent. As for the novel marketing drive, the company won *Advertising Age* magazine's Marketer of the Year Award for 2004. As for its recent comeback, McDonald's is truly lovin' it.

DISCUSSION QUESTIONS

1. Why do firms such as McDonald's need to have a global marketing strategy even though its national menus are localized?
2. What alternative strategy could McDonald's have used to regain its market?
3. For the future, how should McDonald's tap into the convergence among global consumers?

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APPENDIX: THEORIES OF INTERNATIONAL TRADE AND THE MULTINATIONAL ENTERPRISE

Theories are a simplification of complex realities one way or another. A few important theories will be explained here. Each of the theories provides a number of fundamental principles by which you can not only appreciate why international trade and investment occur but also prepare for the next impending change you will probably see in a not-so-distant future. These theories are arranged chronologically so that you can better understand what aspect of the ever-increasing complexities of international business each theory was designed to explain.

Comparative Advantage Theory. At the aggregate level, countries trade with each other for fundamentally the same reasons that individuals exchange products and services for mutual benefit. By doing so, we all benefit collectively. Comparative advantage theory is an arithmetic demonstration made by the English economist, David Ricardo, almost 190 years ago that a country can gain from engaging in trade even if it has an absolute advantage or disadvantage. In other words, even if the United States is more efficient than China in the production of everything, both countries will benefit from mutual trade by specializing in what each country can produce relatively more efficiently.

Let us demonstrate comparative advantage theory in its simplest form: the world is made up of two countries (the United States and China) and two products (personal computers and desks). We assume that there is only one PC model and only one type of desk. We further assume that labor is the only input to produce both products. Transportation costs are also assumed to be zero. **Exhibit 1.3** presents the production conditions and consumption pattern in the two countries before and after trade. As shown, U.S. labor is assumed to be more productive absolutely in the production of both personal computers (PC) and desks than Chinese labor.

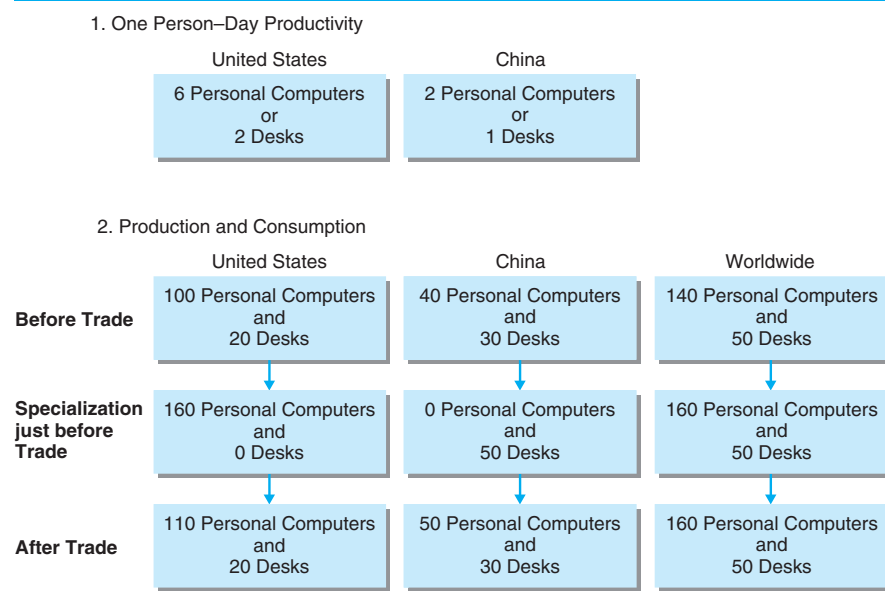
Intuitively, you might argue that since the United States is more productive in both products, U.S. companies will export both PCs and desks to China, and Chinese companies cannot

compete with U.S. companies in either product category. Furthermore, you might argue that as China cannot sell anything to the United States, China cannot pay for imports from the United States. Therefore, these two countries cannot engage in trade. This is essentially the **absolute advantage** argument. Is this argument true? The answer is no.

If you closely look at labor productivity of the two industries, you see that the United States can produce PCs more efficiently than desks compared to the situation in China. The United States has a three-to-one advantage in PCs, but only a two-to-one advantage in desks over China. In other words, the United States can produce three PCs instead of a desk (or as few as one-third of a desk per PC), while China can produce two PCs for a desk (or as many as half a desk per PC). Relatively speaking, the United States is comparatively more efficient in making PCs (at a rate of three PCs per desk) than China (at a rate of two PCs per desk). However, China is comparatively more efficient in making desks (at a rate of half a desk per PC) than the United States (at a rate of one-third of a desk per PC). Therefore, we say that the United States has a **comparative advantage** in making PCs, while China has a comparative advantage in making desks.

Comparative advantage theory suggests that the United States should specialize in production of PCs, while China should specialize in production of desks. As shown in Exhibit 1.3, the United States produced and consumed 100 PCs and 20 desks, and China produced and consumed 40 PCs and 30 desks. As a whole, the world (the United States and China combined) produced and consumed 140 PCs and 50 desks. Now as a result of specialization, the United States concentrates all its labor resources on PC production, while China allocates all labor resources to desk production. The United States can produce 60 more PCs by giving up on the 20 desks it used to produce (at a rate of three PCs per desk), resulting in a total production of 160 PCs and no desks. Similarly, China can produce 20 more desks by moving its labor from PC

EXHIBIT 1-3 COMPARATIVE ADVANTAGE AT WORK



production to desk production (at a rate of half a desk per PC), with a total production of 50 desks and no PCs. Now the world as a whole produces 160 PCs and 50 desks.

Before trade occurs, U.S. consumers are willing to exchange as many as three PCs for each desk, while Chinese consumers are willing to exchange as few as two PCs for each desk, given their labor productivity, respectively. Therefore, the price of a desk acceptable to both U.S. and Chinese consumers should be somewhere between two and three PCs. Let us assume that the mutually acceptable price, or **commodity terms of trade** (a price of one good in terms of another), is 2.5 PCs per desk. Now let the United States and China engage in trade at the commodity terms of trade of 2.5 PCs per desk. To simplify our argument, further assume that the United States and China consume the same number of desks after trade as they did before trade, that is, 20 desks and 30 desks, respectively. In other words, the United States has to import 20 desks from China in exchange for 50 PCs (20 desks times a price of a desk in terms of PCs), which are exported to China from the United States. As a result of trade, the United States consumes 110 PCs and 20 desks, while China consumes 50 PCs and 30 desks. Given the same amount of labor resources, both countries respectively consume 10 more PCs while consuming the same number of desks. Obviously, specialization and trade have benefited both countries.

In reality, we rarely exchange one product for another. We use foreign exchange instead. Let us assume that the price of a desk is \$900 in the United States and 6,300 yuan in China. Based on the labor productivity in the two countries, the price of a PC should be \$300 (at a rate of a third of a desk per PC) in the United States and 3,150 yuan (at a rate of half a desk per PC) in China. As we indicated earlier, U.S. consumers are willing to exchange as many as three PCs for each desk worth \$900 in the United States. Three PCs in China are worth 9,450 yuan. Therefore, U.S. consumers are willing to pay as much as

9,450 yuan to import a \$900 desk from China. Similarly, Chinese consumers are willing to import a minimum of two PCs (worth 6,300 yuan in China) for each desk they produce (worth \$900 in the United States). Therefore, the mutually acceptable exchange rate should be:

$$6,300 \text{ yuan} \leq \$900 \leq 9,450 \text{ yuan, or}$$

$$7.0 \text{ yuan} \leq \$1 \leq 10.5 \text{ yuan.}$$

An actual exchange rate will also be affected by consumer demands and money supply situations in the two countries. Nonetheless, it is clear that exchange rates are determined primarily by international trade.

From this simple exercise, we can make a few general statements or **principles of international trade**.

- Principle 1: Countries benefit from international trade.
- Principle 2: International trade increases worldwide production by specialization.
- Principle 3: Exchange rates are determined primarily by traded goods.

By now you might have wondered why U.S. workers are more productive than Chinese workers. So far we have assumed that labor is the only input in economic production. In reality, we do not produce anything with manual labor alone. We use machinery, computers, and other capital equipment (capital for short) to help us produce efficiently. In other words, our implicit assumption was that the United States has more abundant capital relative to labor than China does. Naturally, the more capital we have relative to our labor stock, the less expensive a unit of capital should be relative to a unit of labor. The less expensive a unit of capital relative to a unit of labor, the more capital we tend to use and specialize in industry that requires a large amount of capital. In other words, the capital–labor endowment ratio affects what type

of industry a country tends to specialize in. In general, a capital-abundant country (e.g., the United States) tends to specialize in capital-intensive industry and export capital-intensive products (personal computers), and import labor-intensive products (desks). Conversely, a labor-abundant country (China) tends to specialize in labor-intensive industry and export labor-intensive products (desks), and import capital-intensive products (personal computers). This refined argument is known as **factor endowment theory** of comparative advantage.

The factor endowment theory can be generalized a bit further. For example, the United States is not only capital-abundant but also abundant with a highly educated (i.e., skilled) labor force. Therefore, it is easy to predict that the United States has comparative advantage in skill-intensive industries such as computers and biotechnology and exports a lot of computers and genetically engineered ethical drugs around the world, and imports manual labor-intensive products such as textiles and shoes from labor-abundant countries such as China and Brazil. **Global Perspective 1-4** clearly shows that labor productivity alone shows a very erroneous impression of industry competitiveness.

Now you might have begun wondering how comparative advantage arguments will help businesspeople in the real world. Suppose you work as a strategic planner for Nike. Shoe manufacturing is extremely labor-intensive, while shoe designing is becoming increasingly high-tech (i.e., skill-intensive). The United States is a relatively skill-abundant and labor-scarce country. Therefore, the country has a comparative advantage in skill-intensive operations but has a comparative disadvantage in labor-intensive operations. There are two ways to use your knowledge of comparative advantage arguments. First, it is easy to predict where competition comes from. Companies from countries like China and Brazil will have a comparative advantage in shoe manufacturing over Nike in the United States. Second, you can advise Nike to establish shoe-manufacturing plants in labor-abundant countries instead of in the labor-scarce United States. As we said earlier, shoe designing has become increasingly high-tech, involving

computer-aided designing and development of light, shock-absorbent material, which requires an extremely high level of expertise. Therefore, based on the comparative advantage argument, you suggest that product designing and development be done in the United States, where required expertise is relatively abundant. Indeed, that is what Nike does as a result of global competitive pressure, and has exploited various countries' comparative advantage to its advantage (no pun intended). Nike has product designing and development and special material development conducted in the United States and has manufacturing operations in labor-abundant countries like China and Brazil.

The comparative advantage theory is useful in explaining inter-industry trade—say computers and desks—between countries that have very different factor endowments. It suggests efficient allocation of limited resources across national boundaries by specialization and trade, but hardly explains business competition, because computer manufacturers and desk manufacturers do not compete directly. Further, it fails to explain the expansion of trade among the industrialized countries with similar factor endowments. Trade among the twenty or so industrialized countries now constitutes almost 60 percent of world trade, and much of it is intra-industry in nature. In other words, similar products are differentiated either physically or only in the customers' minds and traded across countries. Thus, BMW exports its sports cars to Japan, while Honda exports its competing models to Germany. BMW and Honda compete directly within the same automobile industry. This type of intra-industry competition cannot be explained by comparative advantage theory.

International Product Cycle Theory. When business practitioners think of competition, they usually refer to intra-industry competition. Why and how does competition tend to evolve over time and across national boundaries in the same industry? How then does a company develop its marketing strategy in the presence of competitors at home and abroad? **International product cycle theory** addresses all these questions.

GLOBAL PERSPECTIVE 1-4

It is correct to say, “the best way to improve living standards is to encourage investment in sophisticated industries like computers and aerospace.” Is it correct to say, “the best way to improve living standards is to encourage investment in industries that provide high value added per worker”? The real high-value industries in the United States are extremely capital-intensive sectors like cigarettes and oil refining. High-tech sectors that everyone imagines are the keys to the future, like aircraft and electronics, are only average in their value added

Source: Adapted from Paul Krugman, “Competitiveness: Does it Matter?” *Fortune* (March 7, 1994), pp. 109–15.

per worker, but are extremely skill-intensive industries. Look at these statistics:

Value Added Per Worker	Thousands
Cigarettes	\$823
Petroleum refining	\$270
Automobile	\$112
Tires and inner tubes	\$101
Aerospace	\$86
Electronics	\$74
All manufacturing	\$73



Several speculations have been made.⁵⁹ First, a large domestic market, such as the United States, makes it possible for U.S. companies to enjoy **economies of scale** in mass production and mass marketing, enabling them to become lower-cost producers than their competition in foreign countries. Therefore, those low-cost producers can market their products in foreign markets and still remain profitable. In addition, an **economies-of-scope** argument augments an economies-of-scale argument. Companies from a small country can still enjoy economies of scale in production and marketing by extending their business scope beyond their national boundary. For example, Nestlé, a Swiss food company, can enjoy economies of scale by considering European, U.S., and Japanese markets together as its primary market. Second, technological innovation can provide an innovative company a competitive advantage, or **technological gap**, over its competitors both at home and abroad. Until competitors learn about and imitate the innovation, the original innovator company enjoys a temporary monopoly power around the world. Therefore, it is technological innovators that tend to market new products abroad. Third, it is generally the per-capita income level that determines consumers' **preference similarity**, or consumption patterns, irrespective of nationality. Preference similarity explains why intra-industry trade has grown tremendously among the industrialized countries with similar income levels.

Combining these forces with the earlier comparative advantage theory, international product cycle theory was developed in the 1960s and 1970s to explain a realistic, dynamic change in international competition over time and place.⁶⁰ This comprehensive theory describes the relationship between trade and investment over the product life cycle.

One of the key underlying assumptions in the international product cycle theory is that "necessity is the mother of invention." In the United States, where personal incomes and labor costs were the highest in the world particularly in the 1960s and 1970s, consumers desired products that would save them labor and time, and satisfy materialistic needs. Historically, U.S. companies developed and introduced many products that were labor- and time-saving or responded to high-income consumer needs, including dishwashers, microwave ovens, automatic washers and dryers, personal computers, and so on. Similarly, companies in Western Europe tend to innovate on material- and capital-saving products and processes to meet their local consumers' needs and lifestyle orientation. Small and no-frill automobiles and recyclable products are such examples. Japanese companies stress products that conserve not only material and capital but also space to address their local consumers' acute concern about space limitation. Therefore, Japanese companies excel in developing and marketing small, energy-efficient products of all kinds.⁶¹

⁵⁹Mordechai E. Kreinin, *International Economics: A Policy Approach*, 5th ed. (New York: Harcourt Brace Jovanovich, 1987), pp. 276–78.

⁶⁰See, for example, Raymond Vernon, "International Investment and International Trade in the Product Cycle," *Quarterly Journal of Economics*, 80 (May 1966), pp. 190–207; "The Location of Economic Activity," *Economic Analysis and the Multinational Enterprise*, John H. Dunning, ed. (London: George Allen and Unwin, 1974), pp. 89–114; and "The Product Cycle Hypothesis in a New International Environment," *Oxford Bulletin of Economics and Statistics*, 41 (November 1979), pp. 255–67.

⁶¹Vernon, 1979.

International product cycle theory suggests that new products are developed primarily to address the needs of the local consumers, only to be demanded by foreign consumers who have similar needs with a similar purchasing power. As the nature of new products and their manufacturing processes becomes widely disseminated over time, the products eventually become mass-produced standard products around the world. At that point, the products' cost competitiveness becomes a determinant of success and failure in global competition. Your knowledge of comparative advantage theory helps your company identify where strong low-cost competitors tend to appear and how the company should plan production locations.

As presented in **Exhibit 1.4**, the pattern of evolution of the production and marketing process explained in the international product cycle consists of four stages: introduction, growth, maturity, and decline. Let us explain the international product cycle from a U.S. point of view. It is to be reminded, however, that different kinds of product innovations also occur in countries (mostly developed) other than the United States. If so, a similar evolutionary pattern of development will begin from those other industrialized countries.

In the *introductory stage*, a U.S. company innovates on a new product to meet domestic consumers' needs in the U.S. market. A few other U.S. companies may introduce the same product. At this stage, competition is mostly domestic among U.S. companies. Some of those companies may begin exporting the product to a few European countries and Japan where they can find willing buyers similar to U.S. consumers. Product standards are not likely to be established yet. As a result, competing product models or specifications may exist on the market. Prices tend to be high. In the *growth stage*, product standards emerge and mass production becomes feasible. Lower prices spawn price competition. U.S. companies increase exports to Europe and Japan as those foreign markets expand. However, European and Japanese companies also begin producing the product in their own local markets and even begin exporting it to the United States. In the *maturity stage*, many U.S. and foreign companies vie for market share in the international markets. They try to lower prices and differentiate their products to outbid their competition. U.S. companies that have carved out market share in Europe and Japan by exporting decide to make a direct investment in production in those markets to protect their market position there. U.S. and foreign companies also begin to export to developing countries, because more consumers in those developing countries can afford the product as its price falls. Then, in the *decline stage*, companies in the developing countries also begin producing the product and marketing it in the rest of the world. U.S., European, and Japanese companies may also begin locating their manufacturing plants in those developing countries to take advantage of inexpensive labor. The United States eventually begins to import what was once a U.S. innovation.

The international product cycle argument holds true as long as we can assume that innovator companies are not informed about conditions in foreign markets, whether in other industrialized countries or in the developing world. As we amply indicated in Chapter 1, such an assumption has become very iffy. Nor can it be safely assumed that U.S. companies are exposed to a very different home environment from European and Japanese companies. Indeed, the differences among the

EXHIBIT 1-4
INTERNATIONAL PRODUCT CYCLE

	<i>Introduction</i>	<i>Growth</i>	<i>Maturity</i>	<i>Decline</i>
Demand Structure	Nature of demand not well understood Consumers willing to pay premium price for a new product	Price competition begins Product standard emerging	Competition based on price and product differentiation	Mostly price competition
Production	Short runs, rapidly changing techniques Dependent on skilled labor	Mass production	Long runs with stable techniques Capital intensive	Long runs with stable techniques Lowest cost production needed either by capital intensive production or by massive use of inexpensive labor
Innovator Company Marketing Strategy	Sales mostly to home-country (e.g., U.S.) consumers Some exported to other developed countries (e.g., Europe and Japan)	Increased exports to the other developed countries (e.g., Europe and Japan)	Innovator company (e.g., U.S.) begins production in Europe and Japan to protect its foreign market from local competition	Innovator company (U.S.) may begin production in developing countries
International Competition	A few competitors at home (e.g., U.S.)	Competitors in developed countries (e.g., Europe and Japan) begin production for their domestic markets They also begin exporting to the United States	European and Japanese companies increase exports to the United States They begin exporting to developing countries	European and Japanese competitors may begin production in developing countries Competitors from developing countries also begin exporting to the world

Source: Expanded on Louis T. Wells, Jr., "International Trade: The Product Life Cycle Approach," in Reed Moyer, ed., *International Business: Issues and Concepts* (New York: John Wiley, 1984), pp. 5–22.

industrialized countries are reduced to trivial dimensions. Seeking to exploit global scale economies, an increasing number of companies are likely to establish various plants in both developed countries and developing countries, and to cross haul between plants for the manufacture of final products. As an explanation of international business behavior, international product cycle theory has limited explanatory power. It does describe the initial international expansion (exporting followed by direct investment) of many companies, but the mature globetrotting companies of today have succeeded in developing a number of other strategies for surviving in global competition.

Internalization/Transaction Cost Theory. Now that many companies have established plants in various countries, they have to manage their corporate activities across national boundaries. Those companies are conventionally called multinational companies. It is inherently much more complex and difficult to manage corporate activities and market products across national boundaries, rather than from a domestic base. Then why do those multinational companies invest in foreign manufacturing and marketing operations instead of just exporting from their home base? International product cycle theory explains that companies

reactively invest abroad when local competitors threaten their foreign market positions. Thus, the primary objective of foreign direct investment for the exporting companies is to keep their market positions from being eroded. Are there any proactive reasons for companies to invest overseas?

To address this issue, a new strand of theory has been developed. It is known as **internalization** or **transaction cost theory**. Any company has some proprietary expertise that makes it different from its competitors. Without such expertise no company can sustain its competitive advantage. Such expertise may be reflected in a new product, unique product design, efficient production technique, or even brand image itself. As in the international product cycle argument, a company's expertise may eventually become common knowledge as a result of competitors copying it or reverse-engineering its product. Therefore, it is sometimes to an innovator company's advantage to keep its expertise to itself as long as possible in order to maximize the economic value of the expertise. A company's unique expertise is just like any information. Once information is let out, it becomes a "public good"—and free.

In other words, the multinational company can be considered an organization that uses its internal market to produce and distribute products in an efficient manner in situations where the true value of its expertise cannot be

assessed in ordinary external business transactions. Generating expertise or knowledge requires the company to invest in research and development. In most circumstances, it is necessary for the company to overcome this appropriability problem by the creation of a monopolistic internal market (i.e., internalization) when the knowledge advantage can be developed and explored in an optimal manner on a global basis.⁶² The motive to internalize knowledge is generally strong when the company needs to invest in business assets (e.g., manufacturing and marketing infrastructure) that have few alternative uses, uses those assets frequently, and faces uncertainty in negotiating, monitoring, and enforcing a contract. Such a situation suggests a high level of transaction costs due to specific assets and contractual uncertainty involved.⁶³

Resource-Based View and Appropriability Theory.

Now that many companies have established subsidiaries and other affiliates in various countries, they have to manage their far-flung corporate operations to their competitive advantage. The **resource-based view** of the firm suggests that companies can be conceived of as controlling bundles of various resources, also called capabilities. These capabilities are developed through previous experience and over time. When resources are *valuable, rare, difficult to imitate* (inimitable), and *non-substitutable*, they can lead to sustainable competitive advantage.⁶⁴ Resources and capabilities do not only include physical assets but also skills, technologies, and more intangible endowments, such as productive routines and other organizational competencies as well. An individual subsidiary as a resource node or bundle of resources and capabilities with its own unique resource profile plays a significant role in maintaining the multinational company's competitive advantage. Furthermore, its subsidiary's intraorganizational linkages give rise to competitive advantages due to scope and scale economies and other relational benefits.

However, the company's organizational resources can only be sources of sustained competitive advantage if competitors that do not possess these resources cannot obtain them easily. The company's expertise can be channeled through three routes to garner competitive advantage: appropriability regime, dominant design, and operational/marketing capabilities.⁶⁵ **Appropriability regime** refers to aspects of the commercial environment that govern a company's ability to retain its technological advantage. It depends on the efficacy of legal mechanisms of protection, such as patents, copyrights, and trade secrets. However, in today's highly competitive market, legal means of protecting proprietary technology have become ineffective as new product innovations are relatively easily reverse-engineered, improved upon, and invented around by competitors without violating patents and other proprietary

protections bestowed on them. It is widely recognized that the most effective ways of securing maximum returns from a new product innovation are through lead time and moving fast down the experience curve (i.e., quickly resorting to mass production).⁶⁶ Obviously, the value of owning technology has lessened drastically in recent years as the inventor company's temporary monopoly over its technology has shortened.

Dominant design is a narrow class of product designs that begins to emerge as a "standard" design. A company that has won a dominant design status has an absolute competitive advantage over its competition. In an early stage of product development, many competing product designs exist. After considerable trial and error in the marketplace, a product standard tends to emerge. A good case example is Sony's Betamax format and Panasonic's VHS format for VCRs. The Betamax format was technologically superior with better picture quality than the VHS format, but could not play as long to record movies as the VHS. Although the Sony system was introduced slightly earlier than the Panasonic system, the tape's limited capability to record movies turned out to be fatal to Sony as the VHS tape was increasingly used for rental home movies and home recording of movies. Thus, VHS emerged as the worldwide standard for videocassette recording.

Was it simply the act of the "invisible hand" in the marketplace? The answer is clearly no. Panasonic actively licensed its VHS technology to Sanyo, Sharp, and Toshiba for production and supplied VHS-format videocassette recorders to RCA, Magnavox, and GTE Sylvania for resale under their respective brand names.⁶⁷ When Philips introduced a cassette tape recorder, a similar active licensing strategy had been employed for a quick adoption as a dominant standard around the world. Despite various government hurdles to stall the Japanese domination of emerging HDTV technology, Sony is currently trying to make its format a standard by working its way into Hollywood movie studios. It is clear that a wide adoption of a new product around the world, whether autonomous or deliberated, seems to guarantee it a dominant design status.

Operational and marketing ability is in almost all cases required for successful commercialization of a product innovation. The issue here is to what extent this ability is specialized to the development and commercialization of a new product. Indeed, many successful companies have highly committed their productive assets to closely related areas without diversifying into unrelated businesses. This commitment is crucial. Take semiconductor production for example. A director at SEMATECH (a U.S. government-industry semiconductor manufacturing technology consortium established in Austin, Texas, to regain U.S. competitive edge in semiconductor manufacturing equipment from Japanese competition) admits that despite and because of a rapid technological turnover, any serious company wishing to compete on a state-of-the-art computer chip with the Japanese will have to invest a minimum of a billion dollars in a semiconductor manufacturing

⁶² Alan M. Rugman, ed., *New Theories of the Multinational Enterprise* (London: Croom Helm, 1982).

⁶³ Oliver E. Williamson, "The Economics of Organization: The Transaction Cost Approach," *American Journal of Sociology*, 87 (1981), pp. 548–77.

⁶⁴ Jay B. Barney, "Firm Resources and Sustained Competitive Advantage," *Journal of Management*, 17(1, 1991), pp. 99–120.

⁶⁵ David J. Teece, "Capturing Value from Technological Innovation: Integration, Strategic Partnering, and Licensing Decisions," in Bruce R. Guile and Harvey Brooks, eds., *Technology and Global Industry: Companies and Nations in the World Economy* (Washington, D.C.: National Academy Press), pp. 65–95.

⁶⁶ Richard C. Levin, Alvin K. Klevorick, Richard R. Nelson, and Sidney G. Winter, "Appropriating the Returns from Industrial Research and Development," *Brookings Papers on Economic Activity*, 3 (1987), pp. 783–831.

⁶⁷ Richard S. Rosenbloom and Michael A. Cusumano, "Technological Pioneering and Competitive Advantage: The Birth of VCR Industry," *California Management Review*, 29 (Summer 1987), pp. 51–76.

equipment and facility. General Motors invested more than \$5 billion for its Saturn project to compete with the Japanese in small car production and marketing. A massive retooling is also necessary for any significant upgrade in both industries. Furthermore, the software side of manufacturing ability may be even more difficult to match, as it involves such specialized operational aspects as JIT (just-in-time) manufacturing management, quality control, and components sourcing relationships. Irrespective of nationality, those multinational companies that are successful in global markets tend to excel not only in product innovative ability but also in manufacturing and marketing competencies.⁶⁸ It is clear that innovative companies committed to manufacturing and marketing excellence will likely remain strong competitors in industry.

These three sources of competitive advantage are not independent of each other. Given the relative ease of learning about competitors' proprietary knowledge without violating patents and other legal protections, many companies resort to mass production and mass marketing to drive down the cost along the experience curve. To do so requires enormous invest-

ment in manufacturing capacity. As a result, the efficacy of appropriability regime is highly dependent on investment in manufacturing and marketing ability. Similarly, a wide acceptance of a product is most likely necessary for the product to become a dominant design in the world for a next generation of the product. Thus, mass production and marketing on a global scale is likely to be a necessary, if not sufficient, condition for a company to attain a dominant design status for its product.

It is apparent that patents, copyrights, and trade secrets are not necessarily optimal means of garnering competitive advantage unless they are strongly backed by strengths in innovative manufacturing and marketing on a global basis. Likewise, companies strong in manufacturing without innovative products also suffer from competitive disadvantage. In other words, it takes such an enormous investment to develop new products and to penetrate new markets that few companies can go it alone anymore. Thus, to compete with integrated global competitors, an increasing number of companies have entered into strategic alliances so as to complement their competitive weaknesses with their partners' competitive strengths.

⁶⁸Masaaki Kotabe, "Corporate Product Policy and Innovative Behavior of European and Japanese Multinationals: An Empirical Investigation," *Journal of Marketing*, 54 (April 1990), pp. 19-33.

SUMMARY

Three theories that cast some insight into the workings of international business have been reviewed. These theories are not independent of each other. Rather, they supplement each other. Comparative advantage theory is useful when we think broadly about the nature of industrial development and international trade around the world. International product cycle theory helps explain why and how a company initially extends its market horizons abroad and how foreign competitors shape global competition over time and place. Internalization or

transaction cost theory provides some answers to how to manage multinational operations in a very competitive world.

There are other theories to supplement our understanding of international business, however, they are beyond the scope of this textbook and are probably unnecessary. Now you can appreciate how international business has expanded in scope over time. With understanding of these theories, we hope you can better understand the rest of the book.

KEY TERMS

Absolute advantage
Comparative advantage
Commodity terms of trade

Factor endowment theory
International product cycle theory

Economies of scale
Economies of scope
Technological gap

Preference similarity
Internalization theory
Transaction cost theory